Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Special Access Rates for Price Cap	)	WC Docket No. 05-25
Local Exchange Carriers	)	
	)	
AT&T Corp. Petition for Rulemaking to Reform	)	
Regulation of Incumbent Local Exchange Carrier	)	RM-10593
Rates for Interstate Special Access Services	)	

REPLY COMMENTS OF PAETEC HOLDINGS INC.; TDS METROCOM, LLC; U.S. TELEPACIFIC CORP. AND MPOWER COMMUNICATIONS CORP., BOTH D/B/A TELEPACIFIC COMMUNICATIONS; MASERGY COMMUNICATIONS, INC.; AND NEW EDGE NETWORK, INC.

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Dated: February 24, 2010

SUMMARY

I. THRESHOLD MATTERS BEFORE THE COMMISSION

The Initial Comments of the BOCs raise several threshold issues. The BOCs propose certain "overarching principles," including AT&T's contention that reducing special access rates to levels that would be achieved in a competitive market "would affirmatively thwart the Commission's goal in its parallel National Broadband Plan proceeding to encourage investment in higher-capacity broadband alternatives," that should be rejected. AT&T's implicit threat that if deprived of the excessive profits it is earning on special access it will reduce investment in broadband ignores the Commission's obligation to ensure that special access rates must be "just and reasonable." Moreover, ILECs are not the only carriers investing in broadband, and the excessive prices the BOCs charge other carriers for special access deprive those carriers of the capital they need to invest in broadband infrastructure. Indeed, record evidence shows that effective regulation of wholesale prices will increase, rather than decrease, overall investment in high-speed broadband infrastructure.

In light of more than seven years of record evidence demonstrating that its pricing flexibility triggers do not work, the Commission should also reject AT&T's suggestion that before modifying the triggers it must engage in a further time consuming exercise in fact-gathering. The Commission should likewise reject AT&T's claims that before concluding that special access "rates of return" are too high based on ARMIS data, the Commission would have to revisit and reestablish each central aspect of a rate-of-return system through rigorous proceedings and that before modifying the X-factor, the Commission must conduct new, rigorous forward-looking productivity studies.

Consistent with the BOCs' agreement to provide cost and revenue data upon request as a condition of the Commission's grant of forbearance from Section 220(a)(2), the Commission should reject the BOCs' challenge to accounting cost and revenue data that is needed to determine if their special access rates are just and reasonable. Such data is also needed to ascertain whether the BOCs are violating Section 254(k) by unlawfully using non-competitive special access revenues to subsidize competitive broadband services, as suggested by AT&T's claims that a reduction in special access revenues will lead to a reduction in broadband infrastructure.

II. ANSWERS TO THE COMMISSION'S QUESTIONS

(1) Do the Pricing Flexibility Rules Ensure Just and Reasonable Rates?

Contrary to the BOCs' claims, special access prices have increased since the onset of pricing flexibility, leaving aside merger conditions that have recently expired or that are soon to expire. As the NRRI Report concluded, evidence suggests that "sellers are using market power in Phase II areas to raise prices to their large wholesale customers."

A. Are the Pricing Flexibility Triggers an Accurate Proxy for Competition that is Sufficient to Constrain Incumbent LEC Prices?

For two reasons, the pricing flexibility triggers are not an accurate proxy for competition that is sufficient to constrain ILEC prices. First, the BOCs agree with Commenters that the collocation proxy is not reliable. Second, the MSA is too large an area in which to measure the existence of competition. The MSA approach improperly ignores the vantage of the purchaser and whether there are competitive alternatives available to the purchaser in a given location or on a specific transport route between two ILEC wire centers. Building out to reach a building not currently served, apart from physical, legal, and economic obstacles, takes too long. As AT&T

concedes "customers do not want to wait . . . when they need service."[1] As Commenters have shown, the Commission can accomplish a building-by-building or route-by-route analysis with administrative ease.

B. What Analytical Framework Should the Commission Apply so that the Pricing Flexibility Rules Ensure Just and Reasonable Rates?

The Commission should apply its traditional market power analysis to determine where pricing flexibility is warranted by the presence of sufficient competition to constrain the ILEC's market power. Although market share is not necessarily dispositive in itself, this analysis should consider the ILEC's market share. Because the Commission's focus should be on whether special access customers have alternatives to the ILEC and the fact that a competitor may be serving customers elsewhere in an MSA does not mean that it can compete for a particular point-to-point connection, each point-to-point connection should be treated as a separate geographic market. The product market should not include services, such as cable modem services and fixed wireless, that are not considered to be substitutes for special access by more than a limited number of customers. The Commission should reject BOC proposals to undertaking the wasteful and never ending exercise of polling carriers and customers regarding their future "plans" to serve new areas or to engage in self-supply.

(2) Do The Price Cap Rules Ensure Just And Reasonable Rates?

The price caps initialized by the Commission 19 years ago no longer ensure just and reasonable rates. Because price caps were not adopted to permit price cap ILECs to assess unjust and unreasonable rates in perpetuity, it is appropriate for the Commission to evaluate price cap ILECs' costs and profits. Because the Commission already does so for rate-of-return ILECs, it is

[1] AT&T 1/19/10 Comments, at 46.

feasible for it to do so for price cap ILECs. That the BOCs are earning supracompetitive profits and returns from special access is shown by ARMIS data, as well as by comparison with a variety of benchmarks, including forward-looking, cost-based UNE rates, rates offered by competitors, NECA's rate-of-return rates, and even rates offered by Verizon and AT&T to their retail customers for similar services. Although the BOCs contend that the rates-of return shown by ARMIS data are inaccurate, they have not offered any alternative computations.

Rate caps should be reinitialized at cost-based, forward-looking levels. Once they are reinitialized, they should be subject to a productivity-based X-factor and reformed price cap rules.

(3) Do the Commission's Price Cap and Pricing Flexibility Rules Ensure that the Terms and Conditions in Special Access Tariffs and Contracts are Just and Reasonable?

The terms and conditions in special access tariffs and contracts are often unjust and unreasonable. The claims of Verizon and AT&T that such terms are reasonable because customers elected them in a competitive market are circular, and based on assumptions that have been proven by the record to be contrary to fact. The Commission should implement Commenters' suggestions to prohibit certain specified terms and conditions and to adopt more general rules that will minimize BOCs' opportunities to impose new and creative ways of evading the intent of these specific prohibitions.

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NRRI Report	Nat'l Regulatory Research Inst., "Competitive Issues in Special Access Markets, Revised Edition," No. 09- 02, Jan. 21, 2009. *available at* http://nrri.org/pubs/telecommunications/ NRRI_spcl_access_mkts_jan09-02.pdf.
PAETEC *et al.* 1/19/10 Comments or Initial Comments	Comments of PAETEC Holdings Inc.; TDS Metrocom LLC; U.S. TelePacific Corp. and Mpower Communications Corp., both d/b/a TelePacific Communications; Masergy Communications, Inc.; and New Edge Network, Inc., WC Docket No. 05-25, RM-10593 (filed Jan. 19, 2010)
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XO *et al*. 8/8/07 Comments	Comments of XO Communications, LLC, Covad Communications Group, Inc., and NuVox Communications, WC Docket No. 05-25, RM-10593 (filed Aug. 8, 2007)

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REPLY COMMENTS OF
PAETEC HOLDINGS INC.; TDS METROCOM, LLC; U.S. TELEPACIFIC CORP., D/B/A TELEPACIFIC COMMUNICATIONS AND MPOWER COMMUNICATIONS CORP., D/B/A TELEPACIFIC COMMUNICATIONS; MASERGY COMMUNICATIONS, INC.; AND NEW EDGE NETWORK, INC.

PAETEC Holdings Inc., parent company of PAETEC Communications, Inc., McLeodUSA Telecommunications Services, Inc. and various US LEC entities, all of which do business as PAETEC ("PAETEC"); TDS Metrocom LLC; U.S. TelePacific Corp. and Mpower Communications Corp., both d/b/a TelePacific Communications; Masergy Communications, Inc.; and New Edge Network, Inc. (collectively "Commenters"), submit these reply comments in response to the Commission's request that parties comment on the analytical framework necessary to resolve issues in the *Special Access NPRM*.[2]

[2] *Parties Asked to Comment on Analytical Framework Necessary to Resolve Issues in the Special Access NPRM*, Public Notice, WC Docket No. 05-25, RM-10593, DA 09-2388 (rel. Nov. 5, 2009).

I. THRESHOLD MATTERS BEFORE THE COMMISSION

The Commission's objective in this proceeding is to ensure that the price cap and pricing flexibility rules produce just and reasonable rates, as required by Section 201(b) of the Communications Act of 1934, as amended by the Telecommunications Act of 1996 (collectively the "Act"). The Bell Operating Companies ("BOCs") challenge[3] the Commission's invitation[4] that the BOCs voluntarily provide the accounting data needed to determine if their special access earnings exceed reasonable levels. Even without this data, ample record evidence demonstrates price cap and pricing flexibility rates are unreasonable and the existing special access regulatory framework is in dire need of reform. The BOCs attempt to avoid this finding by arguing that the Commission should be guided by certain self-serving overarching principles. For the reasons discussed below, the Commission should reject these principles and require the BOCs to produce their special access accounting data.

(1) The Commission Should Reject the Overarching Principles Advocated by the BOCS

AT&T asserts that "[w]hatever the Commission does in this proceeding should be guided by certain overarching principles, most importantly the need to preserve incentives for broadband investment."[5] AT&T maintains that "mandated rate reductions on those services would affirmatively *thwart* the Commission's goal in its parallel National Broadband Plan

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[3] *See, e.g.*, AT&T 1/19/10 Comments at 10, 49-69; Verizon 1/19/10 Comments, at 43-48; Qwest 1/19/10 Comments, at 44-49.

[4] *Special Access NPRM*, ¶ 29; *see also Parties Asked to Comment on Analytical Framework Necessary to Resolve Issues in the Special Access NPRM*, Public Notice, WC Docket No. 05-25, RM-10593, DA 09-2388, at 5 (rel. Nov. 5, 2009) (stating that "[w]e would expect any analytical framework, based on ARMIS or not, to include specifics as to the measure of profit and reasonableness of that profit").

[5] AT&T 1/19/10 Comments, at 13 (bolding and uppercasing removed).

proceeding to encourage investment in higher-capacity broadband alternatives."[6] Qwest makes a similar argument.[7] AT&T contends that regulating special access rates will thwart ILEC broadband investments because, as Sanford Research found, "'[t]he returns on capital of telecom operators are not very good'" and 'the returns on broadband deployments, even in the dense markets are truly awful.'"[8] AT&T maintains that forcing large rate reductions would deprive ILECs "of the capital needed to continue investing in broadband infrastructure"[9] and that "[t]he Commission should adhere to the first principle of sound regulatory practice, which is to 'do no harm.'" [10]

Contrary to AT&T's assertions, the Commission needs to address *the significant harm* the BOCs are imposing on, end users, competitive carriers, and the United States economy by assessing supracompetitive rates for special access services. While AT&T and Qwest argue that re-regulating special access rates will thwart broadband investment, the fact that BOCs are charging excessive rates to CLECs and wireless carriers for special access services prevents

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[6] *Id*. at 13.

[7] Qwest 1/19/10 Comments, at 20.

[8] AT&T 1/19/10 Comments, at 17 (citing *National Broadband Plan Workshop*, Deployment – Wired Transcript, at 12-13 (Aug. 12, 2009) and quoting Craig Moffett, Sanford Bernstein).

[9] AT&T 1/19/10 Comments, at 17.

[10] *Id*. at 18. AT&T also references the billions of dollars of federal stimulus funds granted and that "constricting the scope of pricing flexibility relief and artificially reducing TDM-based DS1 and DS3 special access prices could only reduce incentives for microwave wireless and cable companies to invest in these areas, and reduce incentives to develop innovative and more efficient market-based solutions to the issue of providing connectivity for broadband services in rural areas." *Id*. at 47-48. AT&T emphasizes again that "mandated rate reductions" would be "contrary to the Commission's goals of fostering competition and broadband deployment (because it would provide incentives for carriers to rely on these lower capacity old-technology facilities rather than on more modern higher capacity facilities offered by the market-based solutions)." *Id*. at 48-49.

CLECs and wireless carriers from investing the excessive amounts they pay the BOCs back into their own companies and further the reach of their own broadband networks. As the record indicates, for the three year period from 2007 through 2009 alone, Economics and Technology, Inc. ("ETI") reported in 2007 that the BOCs excessive prices "will have cost the US economy some 234,000 jobs and roughly $66-billion in economic output."[11]

Moreover, the recently submitted ETI 2/11/10 Report entitled "Regulation, Investment and Jobs, How Regulation of Wholesale Markets Can Stimulate Private Sector Broadband Investment and Create Jobs"[12] demonstrates that the FCC's deregulatory approach, *e.g.*, pricing flexibility for special access, among other things, "has not yielded increased investment by ILECs or CLECs."[13] It explains that "Comprehensive regulation of the rates charged by ILECs for current loop technologies yielded higher levels of investment in loop plant by competitors and by incumbents as well in the past and should be expected to do so in the future."[14] The ETI 2/11/10 Report also "shows that such increased investment, in turn, can be expected to result in significant economic gains and job creation, both within the telecom sector and across the US economy overall."[15]

In addressing ILEC arguments, this ETI report explains that,

> The ILECs' position fails to consider any of the economic benefits of regulation – benefits that include, among other things, making the most efficient use of existing economic assets rather than duplicating them for nothing more than the

[11] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at i; *see also id*. at iii & 7-19.

[12] ETI 2/11/10 Report, at i.

[13] *Id*. at 1 (italics omitted).

[14] *Id*.

[15] *Id*.

> sake of duplication, jump-starting broad-based competition far more quickly than could have been achieved had all entrants been forced to overbuild all existing incumbent networks, encouraging innovation rather than complacency, and the like.[16]

The Report acknowledges that,

> This cost/benefit calculation must be made at two levels – at a microeconomic level (i.e., by each business entity as part of its capital budgeting and investment process) and at a macroeconomic level (by policymakers evaluating the economic merits of alternative regulatory policies). Firms will invest where, from their perspective, such investments will yield a positive return. An entrant will choose to build facilities rather than to purchase wholesale services from the incumbent where (a) this approach is less expensive than buying wholesale services from the incumbent, and (b) the investment can be expected to produce a positive return. By overpricing wholesale services, the incumbent can discourage entrants' use of wholesale services, but if the entrant's cost of acquiring its own facilities is so high that the venture cannot be profitable, the investment will not be made.[17] The incumbents thus focus their policy argument entirely upon (a) and entirely ignore (b). But the empirical evidence of wide scale reductions in telecom investment on the part of both entrants and incumbents following the elimination of price regulation of wholesale services seems to resolve the cost/benefit debate supporting the following conclusion: it was the elimination of regulation, not its imposition, that engendered costs at both the firm (microeconomic) and societal (macroeconomic) levels. Policymakers do not have it within their control to increase revenue opportunities or improve operational efficiencies – but they do have the authority and tools to increase the overall level of competition for broadband facilities.[18]
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> The ETI 2/11/10 Report observes that "[w]ith 'competition unfriendly' regulatory

policies in place, the telecommunications sector has experienced steady and persistent job losses

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[16] ETI 2/11/10 Report, at 6.

[17] For this reason, any BOC arguments that reducing special access rates would deter investment of competitors are fallacious. *See* AT&T 1/19/10 Comments, at 13; Qwest 1/19/10 Comments at 20. Commenters agree with AT&T that the Commission's goal should be to promote "healthiest possible incentives for providers of all types to invest in the broadband infrastructure of the future," AT&T 1/19/10 Comments, at 13, but disagree as to how that should be achieved. Commenters believe that reducing special access rates to reasonable levels would best promote this goals, as well as the goal of developing innovative and more efficient market-based solutions to the issue of providing connectivity for broadband services.

[18] ETI 2/11/10 Report, at 6.

– a drop of more than 400,000 jobs, including the loss of 140,000 jobs at the regional Bell operating companies (RBOCs), between 2001 and 2007."[19] The ETI report finds that investment in broadband telecom infrastructure by both ILECs and CLECs "may be stimulated by adopting a competition-friendly regulation climate, one capable of ensuring that wholesale access to underlying ILEC facilities is and will continue to be made available to entrants that desire to incorporate those wholesale facilities into service offerings of their own."[20] The report explains that "By implementing relatively modest changes to the wholesale telecommunications regulatory environment, the FCC could work towards meeting its goal of encouraging ubiquitous broadband availability and do so using private, not public funds."[21] ETI's "modeling estimates an increase in private sector investment in broadband telecommunications network facilities of as much as $60-billion by the end of 2014 and telecom sector job growth of as much as [450,000] four hundred and fifty thousand American jobs."[22] Referencing its 2007 analysis,[23] ETI further estimates that "additional economy-wide growth off $66-billion and an additional 234,000 jobs over the next five years would also be expected to flow from a reimplementation of several of the FCC's rules that have been dismantled during the last decade."[24]

At bottom, the ET 2/11/10 Report shows that properly regulating special access rates will promote investment that will produce significant economic gains and jobs.[25] The Berkman

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[19] *Id*. at ii.

[20] *Id*. at 22 (italics omitted).

[21] *Id*.; *see also id.* at 31.

[22] *Id*. at 22 (italics omitted); *see also id.* at 31.

[23] ETI 2/11/10 Report, at 33-34.

[24] *Id*. at 22 & 33-34.

[25] *Id*. at 1 (italics omitted).

2/16/10 Final Report provides confirming evidence that based on detailed country-by-country and company-level analyses of the effects of open access and the political economy of regulation on broadband performance, an engaged regulator (unlike the deregulatory approach that the FCC has taken) "contributed to strong broadband performance across a range of metrics."[26]

The Commission should also reject several other overarching principles proposed by the BOCs.[27] AT&T argues that "[a]ny framework the Commission adopts here also must be fact-based and data-driven – which means that the Commission cannot rely on the patently arbitrary types of short-cuts that many regulation proponents have advocated in the past."[28] Commenters concur that any analytical framework needs to be fact-based and data-driven; however, the irony in AT&T's statement is that the pricing flexibility and price cap rules that AT&T supports were themselves the product of arbitrary regulatory short-cuts to deregulation and attaining forward-looking rates, respectively, which have utterly failed. If anything, going forward, the Commission should be more granular in its approach and should not take the regulatory "short cuts" it took in the past. The Commission should, however, move expeditiously to undo the harm resulting from prior rush to deregulate the BOCs.

AT&T further contends that before concluding that the triggers are over-inclusive, the Commission "must actually gather the marketplace facts to determine the real scope of today's

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[26] Berkman 2/16/10 Final Report, at 16 (filed Feb. 16, 2010), *available at* http://cyber.law.harvard.edu/pubrelease/broadband/.

[27] AT&T and Verizon also maintain as threshold matters that the Commission's evaluation of competition in determining the special access analytical framework should be forward-looking and not based on static definitions of products and services. AT&T 1/19/10 Comments at 18; Verizon at 9-30. While Commenters agree that an analytical framework should be forward-looking and not based on static definitions of products and services, Commenters disagree that the Commission should design an analytical framework that is based on potential competition, as Commenters have shown and discuss further herein.

[28] AT&T 1/19/10 Comments, at 19.

competitive networks in order to test those assertions."[29] The Commission has, however, more than seven years of record data that demonstrate the triggers do not work. During this time, the BOCs were allowed to assess supracompetitive prices for special access services to the detriment of competition and the US economy. Gathering further evidence to demonstrate what the record already shows will only: (a) delay any ultimate Commission actions needed to cure the material failures of the price cap and pricing flexibility rules; and (b) permit BOCs to exploit the marketplace further during this delay.

AT&T also avers that before concluding that special access "rates of return" are too high based on ARMIS data, the Commission "would have to revisit and reestablish each central aspect of a rate-of-return system through rigorous proceedings" and that before modifying the X-factor, the Commission "must conduct new, rigorous forward-looking productivity studies."[30] For the reasons discussed below, the BOCs should be able to produce accounting data readily that could be used to reset special access prices. Moreover, as explained herein and previously, the benchmarks and the approaches proposed by Commenters could be used to assist in efficiently setting prices and establishing a new X-factor.

AT&T also submits that the analytical framework must also recognize the importance of "administrative feasibility of any pricing flexibility rules" and that the special access pricing rules need only to be "roughly accurate". [31] AT&T maintains that the Commission "need not achieve granular precision" because "nitpicking at relatively minor mismatches between the

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[29] *Id*. at 19.

[30] *Id*. at 19.

[31] *Id*. at 20.

rules and the marketplace realities would not remotely serve the public interest."[32] AT&T's position is hypocritical. Its assertion that the rules need only to be roughly accurate is inconsistent with its position that any changes to the current special access pricing rules must be supported fully by rigorous fact-based and data-driven analysis and should not implement arbitrary regulatory short-cuts. In any event, the Commenters' proposal, while more granular, is still a rough estimate of marketplace realities and accomplishes administratively feasible reforms to the price cap and pricing flexibility rules that serve the public interest, unlike the current rules which do not.

Finally, AT&T and Qwest argue that advocates of re-regulation have the burden of proof to show that the existing regime should be abandoned.[33] AT&T further contends that "those who advocate more restrictive pricing flexibility rules or price caps bear a heavy burden of proof."[34] AT&T asserts that "rate regulation necessarily imposes very significant costs" and that given "the enormous potential costs from Commission intervention in this functioning marketplace, the Commission could intervene here only if there were overwhelming evidence of a *fundamental* failure in the existing rules."[35] Contrary to these self-serving assertions, while no such burden rests solely on Commenters for re-regulation needed to achieve just and reasonable rates, as mandated by Section 201(b), AT&T fails to provide any empirical evidence of what the "costs" of regulating special access rates would be. Even if it did, as discussed above, the costs would

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[32] *Id*. at 20 (emphasis in original).

[33] Qwest 1/19/10 Comments, at 3, 33, & 39-40; A&T 1/19/10 Comments, at 6 & 20.

[34] AT&T 1/19/10 Comments, at 20.

[35] *Id*. at 20.

surely be significantly less than the enormous costs competitors and the U.S. economy have already incurred and continue to bear if the Commission does not act promptly.

(2) The Commission Should Require the BOCs to Provide the Special Access Cost and Revenue Accounting Data that They Committed to Maintain and Produce Upon Request

The Commission should not tolerate the BOCs' challenge to having accounting cost and revenue data evaluated to determine if their special access rates are just and reasonable. The Commission should require that the BOCs immediately produce such information as they agreed to provide it upon request by the Commission as a condition to granting the BOCs' request for forbearance from cost assignment rules.[36]

Specifically, in granting this relief in 2008, the Commission explained that it still retains the "tools, possibly including accounting data, to accomplish its statutory responsibilities" "under the Act to ensure that rates are just and reasonable, and not unjustly or unreasonably

[36] Specifically, on April 24, 2008 in the *AT&T Cost Assignment Forbearance Order*, the Commission conditionally granted AT&T's and BellSouth's (collectively, AT&T) petitions for forbearance from section 220(a)(2) of the Communications Act of 1934, as amended, and various rules. The grant was expressly conditioned on, among other things, Wireline Competition Bureau (Bureau) approval of a compliance plan that AT&T would file that "describe[ed] in detail how it will continue to fulfill its statutory and regulatory obligations, including sections 272(e)(3) and 254(k), and the conditions of [the *AT&T Cost Assignment Forbearance Order*]." *AT&T Cost Assignment Forbearance Order*, ¶ 31. On September 6, 2008 in the *Verizon/Qwest Cost Assignment Forbearance Order*, the same relief, subject to the same conditions, was extended to Verizon and Qwest. On December 12, 2008 in the *ARMIS Financial Reporting Forbearance Order*, AT&T's, Verizon's and Qwest's request for forbearance from the obligation to file Automated Reporting Management Information System (ARMIS) Reports 43-01, 43-02, and 43-03 was granted, subject to the condition, among others, that these carriers obtained approval of their compliance plans required by the *AT&T Cost Assignment Forbearance Order* and *Verizon/Qwest Cost Assignment Forbearance Order*. The Bureau approved AT&T's, Verizon's and Qwest's compliance plans on December 31, 2008. *See Wireline Competition Bureau Approves Compliance Plans*, Public Notice, WC Docket Nos. 07-21, 07-204, 07-273, DA 08-2827 (W.C.B. Dec. 31, 2008).

discriminatory."[37] The Commission "expressly condition[ed] the forbearance granted…on the provision…of accounting data on request by the Commission for its use in rulemakings, adjudications or for other regulatory purposes."[38] The Commission held that "[t]o the extent that the Commission requests such data", "useable information" must be provided "on a timely basis."[39] The Commission emphasized that a "method of preserving the integrity – for both costs and revenues – of [] accounting systems in the absence of the Cost Assignment Rules" be implemented "to ensure that accounting data requested by the Commission in the future will be available and reliable."[40] The Commission should therefore order the BOCs to produce their special access accounting data.

(3) The Commission Should Require the BOCs to Provide Their Special Access Cost and Revenue Accounting Data to Demonstrate They Are Not Violating Section 254(k)

Section 254(k) of the Act prohibits the BOCs, among others, from "us[ing] services that are not competitive to subsidize services that are subject to competition."[41] Because the regulated

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[37] *AT&T Cost Assignment Forbearance Order*, ¶ 21 (citing 47 U.S.C. §§ 160(a)(1), 201, 202). The Commission noted that "[e]ven without the Cost Assignment Rules, the Act provides the Commission with ample authority – including section 220 – to require AT&T to produce any accounting data that the Commission needs for regulatory purposes, including rulemakings or adjudications, in the future." *Id*.

[38] *AT&T Cost Assignment Forbearance Order*, ¶ 21; *see also id*. at ¶ 45. *see also Verizon/Qwest Cost Assignment Forbearance Order*, ¶ 27 (explaining that in the Commission "extend[s] to Verizon and Qwest forbearance from the Cost Assignment Rules to the same extent granted AT&T in the *AT&T Cost Assignment Forbearance Order* and subject to the same conditions"); *ARMIS Financial Reporting Forbearance Order*, ¶ 12.

[39] *AT&T Cost Assignment Forbearance Order*, ¶ 21.

[40] *Id*.

[41] 47 U.S.C. § 254(k).

special access services for BOCs and certain ILECs only include TDM-based services,[42] the record suggests that the BOCs could be unlawfully using their regulated TDM-based special access service revenues to subsidize their packet-based broadband network deployments and services.[43]

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[42] *See, e.g.*, Verizon Telephone Companies' Petition for Forbearance from Title II and *Computer Inquiry* Rules with Respect to their Broadband Services Is Granted by Operation of Law, WC Docket No. 04-440, News Release (rel. Mar. 20, 2006), *review denied, Sprint Nextel Corp. v. FCC*, 508 F.3d 1129 (D.C. Cir. 2007); Petition of the Verizon Telephone Companies For Forbearance, WC Docket No. 04-440 (filed Dec. 20, 2004); *Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Its Broadband Services, Petition of BellSouth Corporation for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Its Broadband Services*, WC Docket No. 06-125, Memorandum Opinion and Order, 22 FCC Rcd 18705, ¶ 13 (2007) (subsequent history omitted); *Petition of the Embarq Local Operating Companies for Forbearance Under 47 U.S.C. § 160(c) from Application of Computer Inquiry Rules and Certain Title II Common-Carriage Requirements, Petition of the Frontier and Citizens ILECs for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Their Broadband Services*, WC Docket No. 06-147, Memorandum Opinion and Order, 22 FCC Rcd 19478, ¶ 12 (2007) (granting in part Embarq's and Frontier/Citizen's requests for forbearance relief comparable to the relief granted Verizon through operation of law) (subsequent history omitted); *Qwest Petition for Forbearance Under 47 USC Section 160(c) from Title II and Computer Inquiry Rules with Respect to Broadband Services*, 23 FCC Rcd 12260, ¶ 13 (2008).

[43] While the FCC in the *Wireline Broadband Internet Access Services Order* did not require LECs to "classify their non-common carrier, broadband Internet access transmission operations as nonregulated activities under part 64," the FCC recognized that "[c]lassifying those operations as regulated under part 32 means that any necessary ratemaking adjustments, including any reallocations of costs, will be addressed in the ratemaking process." *Wireline Broadband Internet Access Services Order*, ¶ 135. It further stated that "some price cap carriers treat broadband special access services as price cap services, while others treat these broadband services as services excluded from price caps" and that "[p]rice cap carriers that have tariffed these services under price caps, and that choose to replace these tariffed services with non-common carriage arrangements, will make the appropriate adjustments to the actual price index (API) and price cap index (PCI) for the special access basket." *Wireline Broadband Internet Access Services Order*, ¶ 135. The FCC explained that "[t]he ordinary application of the price cap rate formulas will ensure that other special access rates remain consistent with the price cap rules after deregulation of broadband transmission services" and that "[c]arriers that have excluded broadband transmission services from price caps will not need to make these adjustments." *Id.* Nothing in the record indicates, however, that the BOCs have or were not required to make the requisite adjustments and are not otherwise violating Section 254(k).

AT&T maintains that forcing large rate reductions would deprive ILECs "of the capital needed to continue investing in broadband infrastructure"[44] and that "[t]he Commission should adhere to the first principle of sound regulatory practice, which is to 'do no harm.'"[45] AT&T has made similar claims in *ex partes* filed that "slashing special access rates" would deprive ILECS of revenues needed to deploy next generation facilities.[46]

BOCs should not be permitted to justify higher regulated DS1 and DS3 special access rates to cover their costs of deploying such non-regulated mass market broadband services. It appears that AT&T is admitting that it is doing just that and wants the Commission to condone such cross subsidizations that Section 254(k) prohibits. Indeed, ETI reports that "ARMIS almost certainly understates rates of return for [s]pecial access and other regulated services because RBOC capital expenditures for unregulated broadband and video services are primarily assigned

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[44] AT&T 1/19/10 Comments, at 17.

[45] *Id*. at 18. As previously noted, AT&T also references the billions of dollars of federal stimulus funds granted and that "constricting the scope of pricing flexibility relief and artificially reducing TDM-based DS1 and DS3 special access prices could only reduce incentives for microwave wireless and cable companies to invest in these areas, and reduce incentives to develop innovative and more efficient market-based solutions to the issue of providing connectivity for broadband services in rural areas." *Id*. at 47-48. AT&T emphasizes again that "mandated rate reductions" would be "contrary to the Commission's goals of fostering competition and broadband deployment (because it would provide incentives for carriers to rely on these lower capacity old-technology facilities rather than on more modern higher capacity facilities offered by the market-based solutions)." *Id*. at 48-49.

[46] *See* Letter from Frank S. Simone, Assistant Vice President, Federal Regulatory, AT&T Services, Inc., to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, pdf p. 6 of 8 (filed Nov. 4, 2009) (stating that "Slashing ILEC special access rates would: Deprive ILECs of revenue used to invest in next generation facilities…"); *see also* Letter from Frank S. Simone, Assistant Vice President, Federal Regulatory, AT&T Services, Inc., to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, 1-2 (filed Oct. 9, 2009) (explaining that "reducing ILEC special access rates on legacy TDM-based DS1 and DS3 services will lead to less - not more - broadband infrastructure investment…"); *see also* Letter from Melissa Newman, Vice President Federal Relations, Qwest, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, at 14 (pdf page 15) (filed Oct. 28, 2009) (stating that "lowering prices of TDM-based services may have the unintended consequences of lowering investment in, and adoption of fiber technologies").

to regulated services investment categories – including the special access category – while the revenues generated by these services are primarily recorded to the unregulated category."[47] ETI explains that "[t]he resulting mismatch of understated broadband revenues and overstated broadband costs (two key components of the rate of return calculation) consistently and systematically understate the rates of return for regulated services – special access in particular."[48] ETI's analysis reveals that the BOCs "[i]nvestment made to provide unregulated services is inappropriately allocated to the interstate special access category – suppressing reported earnings"[49] and AT&T's and Verizon's "Increase[s] in 'Non-Regulated' Plant in Service as Reported in ARMIS Do[] Not Begin to Cover the Total Broadband Investment During the Comparable Period: 2003 – 2007."[50] ETI concludes that "[e]xcluding *FiOS* and *Lightspeed* outlays from Verizon and AT&T special access rate of return calculations would substantially increase the results."[51] AT&T's statement that forcing large rate reductions would deprive ILECs "of the capital needed to continue investing in broadband infrastructure"[52] along with ETI's conclusions, justify an investigation into whether the BOCs are in fact violating Section 254(k).

In determining whether the BOCs' special access rates are just and reasonable, the Commission should also make a determination as to whether the BOCs are using their excessive earnings associated with regulated special access services to subsidize their unregulated

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[47] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 20 (italics removed).

[48] *Id*.

[49] *Id*. at 20 (bolding removed).

[50] *Id*. at 23-24 (bolding removed).

[51] *Id*. at 25 (bolding removed).

[52] AT&T 1/19/10 Comments, at 17.

broadband deployment and services. Accordingly, the Commission should require the BOCs to provide all special access cost and revenue accounting data that is needed to determine if the BOCs are violating Sections 254(k) and 201(b) of the Act.[53]

II. ANSWERS TO THE COMMISSION'S QUESTIONS

(1) Do the Pricing Flexibility Rules Ensure Just and Reasonable Rates?

As Commenters demonstrated in their Initial Comments,[54] the pricing flexibility rules have produced supracompetitive rates, rather than the just and reasonable rates reflective of a competitive market. The Commission has long recognized that the level of competition in a market can be determined based on whether there have been "*substantial* and *sustained* price

[53] In granting the BOCs' request for forbearance from the cost assignment rules, the Commission expressly required the BOCs to provide cost accounting information necessary to show their compliance with Section 254(k). *AT&T Cost Assignment Forbearance Order*, ¶ 30; *see also Verizon/Qwest Cost Assignment Forbearance Order*, ¶ 27 (explaining that in the Commission "extend[s] to Verizon and Qwest forbearance from the Cost Assignment Rules to the same extent granted AT&T in the *AT&T Cost Assignment Forbearance Order* and subject to the same conditions"). The BOCs have committed to providing this information upon request. *See* Letter from Linda Vandeloop, Director - Federal Regulatory, AT&T Services Inc., to Julie A. Veach, Acting Bureau Chief, Wireline Competition Bureau, FCC, WC Docket Nos. 07-21 & 05-342, at 2 (filed July 24, 2009) (attaching AT&T's annual 254(k) compliance certification that states, among other things, that certain AT&T operating telephone companies "will provide any cost accounting information necessary to prove such compliance in accordance with any lawful request for same made by the Commission."); Letter from Melissa E. Newman, Vice President – Federal Regulations, Qwest Communications International inc., to Sharon Gillett, Chief, Wireline Competition Bureau, WC Docket No. 07-204, 07-21, at 2 (filed Sep. 24, 2009) (attaching 254(k) certification that states, among other things, "Qwest Corporation will maintain and provide to the FCC any cost accounting information necessary to establish such compliance if appropriately requested to provide such information."); Letter from Ann Berkowitz, Director, Federal Regulatory, Verizon, to Marlene H Dortch, Secretary, FCC, WC Docket No. 07-273 (filed Sep. 18, 2009)) (attaching its annual 254(k) compliance certification that states, among other things, Verizon incumbent local exchange carriers will maintain and provide to the FCC any cost accounting information necessary to establish such compliance if appropriately requested to provide such information").

[54] PAETEC *et al.* 1/19/10 Comments, at 2-10;

increases."[55] As demonstrated in earlier comments, the Commission's Phase II pricing flexibility tests incorrectly identify where competition is sufficient to constrain prices because significant record evidence demonstrates the BOCs have in most cases,[56] absent merger condition obligations, been raising prices on various term lengths (especially basic monthly and 1-2 year terms)[57] throughout MSAs where they have been granted Phase II pricing flexibility.[58]

The BOCs continue to argue that to the contrary, special access prices have decreased since the onset of pricing flexibility. In particular, the BOCs contend that their average or what they are characterize as "real" special access prices for DS1 and DS3 services have declined.[59] Their assertions, like those they made in 2005 and 2007, rest upon misleading "analyses" that

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[55] *Special Access NPRM*, ¶ 73 (emphasis in original).

[56] PAETEC *et al.* 1/19/10 Comments, at 2-10; Sprint 1/19/10 Comments, at 34-35; NoChokePoints 1/19/10 Comments, at 18-20; Global Crossing 1/19/10 Comments, at 4-8; ATX *et al.* 8/8/07 Comments, at 5-6 & 9-11, Attachment 4; AD Hoc 8/8/07 Comments, Appendix 2: Declaration of Susan M. Gately, ¶¶ 17-19 & Exhibits 1-3; Sprint 8/8/07 Comments, Attachment 2: Declaration of Bridger M. Mitchell, ¶¶ 54-58 & Exhibit 1; Global Crossing 8/8/07 Comments, Declaration of Janet S. Fischer, ¶ 5 & Tables 1-4; ATX *et al.* 7/29/05 Comments, at 14-19; Ad Hoc 6/13/05 Comments, Declaration of M. Joseph Stith; COMPTEL *et al.* 6/13/05 Comments, Declaration of Janet S. Fischer; ATX *et al.* 6/13/05 Comments, at 10-13; GAO Report, at 28.

[57] In Table 3 on page 8 of the PAETEC *et al.* 1/19/10 Comments, the AT&T-MI (after 6/30/10) pricing flexibility rate was referenced as $534.00 with a percent above the NECA rate of 144.58%. The rate should have been $527.00 with a percent above the NECA rate of 141.38%. A revised version of Exhibit 1 attached to PAETEC *et al.* 1/19/10 Comments is attached hereto as Exhibit 1 that includes that figure and notes other miscellaneous changes made to the previously filed Exhibit 1.

[58] Notably, the Commission recognizes that "a substantial price increase need not be a large increase" but can be a "small but significant non-transitory price increase in the relevant product market." *Special Access NPRM*, n.188. As previously explained (*see* ATX *et al.* 6/13/05 Comments, at 11), to the extent BOCs have not increased their special access rates and have kept them at pre-pricing flexibility levels, the fact that BOCs are maintaining such rate levels is "tantamount to a price *increase* in light of the declining costs of special access service…." *See* Ad Hoc 6/13/05 Comments, Declaration of M. Joseph Stith, ¶ 17.

[59] *See, e.g.*, Verizon 1/19/10 Comments, at 5-8; AT&T 1/19/10 Comments, at 25 & Exhibit A: Declaration of Dennis W. Carlton and Hal S. Sider, ¶ 51-55; Qwest 1/19/10 Comments, at 9, Declaration of Timothy J. Tardiff and Dennis L. Weisman, ¶¶ 15-18 & 20-21.

have been fully refuted.[60] As Dr. Selwyn previously demonstrated, these analysis are flawed because, among other things, the BOCs inappropriately (1) "substitute 'average revenue' for actual prices";[61] (2) treat shifts of relative demand from month-to-month to anticompetitive and customer-constraining term and volume contracts as reflecting price changes; (3) "combine price changes for price capped special access services with pricing flexibility services and interpret price decreases in price capped special access services as decreases for services for which the [BOC] has pricing flexibility"; and/or (4) "treat mere relative shifts in demand for circuit-mileage as price changes."[62] Moreover, because the wired telecommunications sector has experienced more productivity increases year-over-year than the economy as a whole,[63] the price-adjustment to account for inflation made by Verizon[64] and Qwest[65] has no place in such a comparison. Any comparisons of actual rates must account for this additional productivity.

Qwest further contends that the actual rates customers pay, and not the rack rate list

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[60] *See* WILTEL 7/29/05 Comments, Exhibit 7: Reply Declaration of Lee L. Selwyn, ¶¶ 33-55; *see also* Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at A-22 through A-26.

[61] *See* WILTEL 7/29/05 Comments, Exhibit 7: Reply Declaration of Lee L. Selwyn, at ii.

[62] *See id*. at ¶ 54; *see also id.* ¶¶ 33-54; *see also* Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at A-22 through A-26.

[63] *See, e.g., LEC Price Cap Order*, ¶ 75; PAETEC *et al.* 1/11/10 Comments, at 62-63; ATX *et al.* 8/8/07 Comments, at 20-21; ATX *et al.* 7/29/05 Comments, at 45; ATX *et al.* 6/13/05 Comments, at 24-25.

[64] Verizon 1/19/10 Comments, at 50-51 & Attachment B: Declaration of Harold E. West, ¶ 7.

[65] Qwest 1/19/10 Comments, Declaration of Timothy J. Tardiff and Dennis L. Weisman, ¶ 21.

prices, are the appropriate starting point for any pricing analysis.[66] As explained above, substantial evidence in the record shows, however, that BOCs' "actual" special access prices have in most cases generally increased (especially basic monthly and 1-2 year terms) absent the AT&T/SBC, Verizon/MCI and AT&T/BellSouth merger conditions.[67] Moreover, as COMPTEL explained, rack rates are pertinent to evaluating the effective rates that customers pay.[68]

Verizon goes on to mischaracterize the GAO Report and states that it found that "between 2001 and 2005, consumers of special access services have paid less for DS1 and DS3 special access services, both in the areas where pricing flexibility has been granted and in the areas that remain subject to price cap regulation."[69] Verizon fails, however, to consider the GAO's express finding that "prices and average revenues are higher, on average, in phase II MSAs—where competition is theoretically more vigorous—than they are in phase I MSAs or in areas where prices are still constrained by the price cap."[70] Verizon and Qwest cite the NRRI report's finding that prices for both DS1 and DS3 services declined between 2006 and 2007.[71] Verizon and Qwest fail to acknowledge NRRI's ultimate finding — that "[o]verall evidence fails to support a conclusion that sellers are being restrained in Phase II areas by competition to offer lower prices. Instead, [evidence] suggests the contrary conclusion, that sellers are using market

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[66] Qwest 1/19/10 Comments, Declaration of Timothy J. Tardiff and Dennis L. Weisman, at n.12.

[67] Qwest contends that rack rates have declined in recent years and cites the *USTelecom Report* for this proposition. Qwest 1/19/10 Comments, at 9-10. Qwest fails to note that asserted declines were likely triggered by the AT&T/BellSouth merger conditions the FCC imposed on AT&T and were not prompted by competition.

[68] *See* COMPTEL 1/19/10 Comments, at 15-21 (explaining why the Commission should use rack rates in performing the price/cost analysis).

[69] Verizon 1/19/10 Comments, at 7.

[70] GAO Report, at 13.

[71] Verizon 1/19/10 Comments, at 7; Qwest 1/19/10 Comments, at 9.

power in Phase II areas to raise prices to their large wholesale customers."[72]

If, as the BOCs claim, special access prices have been dropping where they received phase II pricing flexibility, they should be able to show via a direct "apples-for-apples" comparison of actual tariff prices at various points in time,[73] rather than by means of the indirect and inapposite device of an average revenue surrogate.[74] The direct comparisons, submitted by special access purchasers on numerous occasions in this proceeding, disprove the BOCs' claims and show that phase II pricing flexibility rates reflect substantial and sustained price increases. It is hardly surprising the BOCs needed to devise this "'smoke and mirrors' approach to 'prove' what in fact is not true."[75]

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[72] NRRI Report, at 66.

[73] For AT&T and Verizon, such a comparison should have been prepared during the times before applicable merger conditions forced pricing reductions and/or prohibited rate increases. Moreover, AT&T's tariffs demonstrate that once the merger conditions sunsets on June 30, 2010, critical Phase II pricing rates are already scheduled to shoot up above AT&T's regulated price cap rates. *See* PAETEC *et al.* 1/19/10 Comments, at 8.

[74] WILTEL 7/29/05 Comments, Reply Declaration of Lee L. Selwyn, ¶¶ 38 & 46.

[75] WILTEL 7/29/05 Comments, Reply Declaration of Lee L. Selwyn, ¶ 46. As Dr. Selwyn previously observed, the all-important question is why do the BOCs "*still* choose to use special access revenue as a proxy of actual prices when such pricing data is available in [their] tariffs." *See* WILTEL 7/29/05 Comments, Reply Declaration of Lee L. Selwyn, at ii. The answer is simple: "actual prices for special access services subject to pricing flexibility have gone up or been artificially support at supra-competitive levels, and the only way to view the situation any differently is to ignore and obscure the facts." *See* WILTEL 7/29/05 Comments, Reply Declaration of Lee L. Selwyn, at ii.

A. Are the Pricing Flexibility Triggers an Accurate Proxy for Competition that is Sufficient to Constrain Incumbent LEC Prices?

The Commenters demonstrated that the pricing flexibility triggers, which are based on collocation of competitive carriers in ILEC wire centers throughout an MSA, are not an accurate proxy for the kind of sunk investment by competitors sufficient to constrain ILEC special access prices for channel terminations and dedicated transport facilities. As explained below, the BOCs' recently filed comments do not support any other conclusion.

1. Collocation is Not a Reliable Proxy to Identify Competition Sufficient to Constrain ILECs from Misusing Market Power

Contrary to the Commission's findings in the *Pricing Flexibility Order*, for the numerous reasons Commenters and other parties have provided,[76] the extent of collocation in an MSA under the pricing flexibility rules is not a reliable of indicator of the level of competition in the special access market needed to deter exclusionary pricing behavior within that MSA. While Verizon and AT&T agree with Commenters that pricing flexibility collocation triggers are not reliable proxies to identify competition, they argue that the collocation triggers are underinclusive because: (1) they exclude wireline competitors that bypass ILEC facilities completely and serve customers that are located in a wire center's service area but do not collocate in the wire center; (2) they do not account for intermodal competitors (cable, wireless, microwave) that typically have no need to collocate in an ILEC wire center;[77] and/or (3) Phase II

[76] *See, e.g.*, PAETEC *et al.* 1/19/10 Comments, at 13-16; NoChokePoints 1/19/10 Comments, at 15-16; Sprint 1/19/10 Comments, at 33-34.

[77] In pointing to PAETEC as a "fixed wireless provider" that "offer[s] service in various locations" and "serves over 84 of the top 100 Metropolitan Statistical Areas," Verizon grossly overstates the extent to which PAETEC is able to compete with BOCs without being collocated in a BOC wire center. Verizon 1/19/10 Comments, at 23-27 & Attachment A: Declaration of Michael D. Topper, ¶ 31 and n.52. In fact, PAETEC serves a very small percentage of its end

channel termination triggers were set too high at the outset.[78]

The BOCs' arguments, along with Commenters' criticisms, demonstrate the collocation proxy is not reliable, and that a better approach should be adopted. As Commenters explained, rather than engage in pure speculation as to whether competition exists to justify granting pricing flexibility by using the current flawed collocation triggers, a refined and more granular test should be applied. The more granular test should look at whether actual competitive facilities are: (1) available to a given location or on a particular route and (2) able to constrain the BOCs' special access prices.

Despite the identified material flaws with the triggers, Qwest and AT&T ask that the Commission stop to determine whether the current collocation triggers are fair proxies for facilities based competition.[79] Given the criticisms, the existing collocation triggers are not

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user locations via fixed wireless technology. *See* Reply Declaration of William A. Haas (attached hereto as Exhibit 2), ¶¶ 4- 5.

[78] AT&T 1/19/10 Comments, at 28-38; Verizon 1/19/10 Comments, at 20. As to point (3), AT&T asserts that "[t]here are many areas throughout the country where competitors have deployed significant sunk facilities that compete directly with the incumbent special access but where incumbents have not attained phase II pricing flexibility for channel terminations because they do not quality for relief under the existing triggers," for example New York. AT&T 1/19/10 Comments, at 37; *see* Verizon 1/19/10 Comments, Attachment A: Declaration of Michael D. Topper, ¶ 11. AT&T asks that because of the shortcomings of the collocation triggers, the Commission develop "an alternative or supplement (*e.g.*, business lines or a demonstration that a cable or other intermodal provider is actually providing channel terminations in the area in question) to the collocation-based triggers." AT&T 1/19/10 Comments, at 38.

[79] *See, e.g.*, Qwest 1/19/10 Comments, at 6 & 25-26, 39-40; AT&T 1/19/10 Comments, at 4. AT&T also asserts that the "[t]he Phase I triggers are likewise set too high" and "the Commission could rationally grant nationwide Phase I relief to all price cap ILECs in all areas." *See* AT&T 1/19/10 Comments at 38. This argument strains credulity because AT&T does not require Phase I relief to reduce its special access prices, rather it apparently seeks the ability to lock customers into anticompetitive special access contracts. Requests such as this should be rejected because they are premised on the faulty view that the special access market is sufficiently competitive to permit reliance on competitive forces, rather than regulation, to assure reasonable prices, terms and conditions. As the record reveals and as found by every regulatory

reliable proxies to identify competition sufficient to constrain ILECs from misusing market power. Therefore, the Commission should not expend its limited resources and generate further delay while engaging in additional evaluation of the current unreliable proxy.[80]

2. The MSA is an Inappropriate Geographic Area in which to Grant Pricing Flexibility

Nor should the Commission continue to use the MSA as the geographic area in which to grant pricing flexibility. As Commenters have explained,[81] in conducting a competitive analysis, the relevant geographic market is an "area in which all customers in that area will likely face the same competitive alternatives for a product."[82] An MSA is far too large an area to grant pricing

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authority that has looked at the matter, including the Commission, DOJ, and even GAO, BOCs control last mile access to the vast majority of customer locations. Therefore, there is no basis for relaxing the Commission's already too deregulatory program of special access oversight. *See* 360 *et al.* 8/15/07 Comments, at 33-36 (explaining that the Commission should reject all BOC proposals to relax rules governing special access). Rather, as discussed herein and in Initial Comments, a modified analytical framework and further regulation as proposed is warranted.

[80] When the Commission adopted the collocation triggers in the Pricing Flexibility Order, DS1 through OCn UNE loops and transport were available on an unlimited basis and therefore there was continuous downward pressure on special access rates. The Commission likely believed that collocation would be sufficient proxy because if it was unreliable, the availability of Section 251(c)(3) UNEs that were available to all carriers, *i.e.*, CLECs, wireless and interexchange carriers, would serve as a safeguard to discipline special access prices. As the Commission recognizes, UNEs are no longer available for the exclusive provision of mobile wireless or interexchange services. *See* 47 C.F.R. § 51.309(b). Moreover, the *TRO* and *TRRO* dramatically reduced the Section 251(c)(3) UNEs that ILECs must offer to CLECs and even the DS1 and DS3 UNEs that are still available as UNEs are no longer available everywhere to CLECs if certain caps or *TRRO* non-impairment thresholds are met. Given these limitations, the availability of UNEs cannot be relied on as a safeguard to force the ILECs to reduce their special access rates to competitive levels.

[81] *See* PAETEC *et al.* 1/19/10 Comments, at 16.

[82] *Applications of Ameritech Corp. and SBC Communications Inc. for Consent to Transfer Control*, WC Docket No. 98-141, Memorandum Opinion and Order, 14 FCC Rcd 14712, ¶ 69 n.147 (1999) (citation and history omitted); *see also Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace*, 12 FCC Rcd 15756, ¶ 28 (1997) (explaining that the FCC determines the relevant geographic market by considering whether, if

flexibility because within an MSA, competitive conditions vary widely.[83] Thus, for example, competition in one part of an MSA will not constrain ILEC special access pricing in another geographic area within the same MSA.[84] The BOCs assert, however, that the Commission need not define an ideal geographic market and should continue to analyze competition by MSAs.[85] While Verizon states that "the Commission should not let the 'perfect' be the enemy of the good",[86] record evidence indicates that there is nothing "good" or rational about using the MSA, which is far too large, as the geographic area within which to gauge effective competition.

Verizon maintains that the MSA is appropriate because "[m]any of the service arrangements that are in place today between incumbent carriers and customers were developed and negotiated on the basis of the current MSA-based regime."[87] It asserts that "[u]sing the current MSA-based regime for purposes of analyzing competition would be more consistent with the manner in which competitors market and deploy their high capacity services."[88] AT&T

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all carriers raised their prices in a specific area, a customer would be unable to find the same service in another area at a lower price).

[83] *See, e.g., TRRO,* ¶ 155; *see also* Reply Comments of WorldCom, Inc., RM-10593, at 9-10 (filed Jan. 23, 2003).

[84] Sprint 8/8/07 Comments, Attachment 2: Declaration of Bridger M. Mitchell, ¶¶ 27-28.

[85] Verizon 1/19/10 Comments, at 30; AT&T 1/19/10 Comments at 44-47; Qwest 1/19/10 Comments, at 26-30.

[86] Verizon 1/19/10 Comments, at 30.

[87] Verizon 1/19/10 Comments, at 31.

[88] *Id*. In support, Verizon asserts that "PAETEC claims it can 'reach 100% of its MSA coverage area via Ethernet utilizing existing partnership agreements.'" *Id.* This substantially overstates the extent of PAETEC's ability to serve end users throughout an MSA without using BOC facilities, as the vast majority of PAETEC's end user connections are provided by the BOCs. *See* Exhibit 2 Reply Declaration of William A. Haas, ¶¶ 4-6. Thus, PAETEC's ability to serve a new customer in a building in which PAETEC does not already have its own fiber is almost entirely dependent on its use of BOC facilities. *Id*. ¶¶ 5-7. Verizon's assertion that PAETEC is one of "multiple competitive fiber suppliers throughout each of the top 25 MSAs,"

maintains that: (i) because "special access demand is overwhelmingly concentrated,"[89] reducing the geographic scope "would add considerable complexity to the rules for likely very little benefit";[90] (ii) even if there are pockets where no competition exists, because ILECs must file the negotiated contracts and tariffs, all special access purchasers throughout a MSA can gain the benefit of negotiated rate reductions that result from competition, which typically apply throughout a MSA;[91] (iii) "tariffed prices for special access rate elements… typically do not vary much within an MSA";[92] and (iv) a more granular approach would have "no discernable benefit."[93] Qwest also avers that (i) "with occasional exceptions, the pricing options available to ILEC customers on all point-to-point routes throughout an individual MSA are essentially uniform, and the pricing ILECs offer for their special access services do not vary from route to route or among wire centers in an MSA";[94] and (ii) "competing providers typically deploy their fiber rings or other facilities over broad geographic areas in order to address demand across that entire area."[95]

These contentions can be rejected readily as they turn the competitive analysis of whether facilities-based competition exists on its head. These arguments do not take into account the competitive alternatives to a ILEC's channel termination that are actually available to a

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Verizon 1/19/10 Comments, at 19, is also highly misleading and substantially overstates the extent to which PAETEC has its own fiber in the top 25 MSAs. *Id*. ¶ 7.

89 AT&T 1/19/10 Comments, at 44.

90 *Id*.

91 *Id*.

92 *Id*. at 45.

93 *Id*.

94 Qwest 1/19/10 Comments, at 27-28.

95 *Id*. at 28.

purchasing customer located in a specific building within a serving wire center, let alone an MSA. The MSA approach improperly ignores the vantage of the purchaser and whether there are competitive alternatives available to the purchaser in a given location or on a specific transport route between two ILEC wire centers. If there are no competitive options available to a purchaser in a MSA, a test that finds competition exists to that purchaser is ludicrous.

In addition, the BOCs' arguments proceed from the flawed premise that because BOC pricing is generally uniform, the existence of competition on one route or for one building will force prices down to the competitive level on all routes and for all buildings. That logic is completely flawed and ignores the market power that BOCs wield. Indeed, given the very low level of competition in most MSAs, let alone the limited competition on individual routes or for channel terminations, the opposite is more likely to be true: the BOC is able to impose monopoly pricing throughout an MSA, even if that means losing some market share in the limited locations where competitive alternatives exist, rather than foregoing monopoly rents in the vast majority of locations where competitive alternatives do not exist. BOCs are so empowered because their monopoly on the majority of routes and channel terminations enables them to impose anticompetitive terms and conditions (*e.g.*, minimum revenue commitments, percentage of spend, limitation on use of high capacity UNEs) that effectively prohibit CLECs from using alternatives even when they do exist in those few areas.

As Sprint explained, "[e]ven if the incumbent LEC charges a uniform price throughout an MSA or a region, it can still set that uniform price at a level that allows it to exploit the lack of competition in some parts of the MSA or region."[96] In these circumstances, the ILEC "can maximize its profits by setting a uniform region-wide price that is supra-competitive, but that

[96] Sprint 1/19/10 Comments, at 32.

accounts for the presence of competition in some areas within the region."[97] Thus, a uniform price fails to "protect consumers in less competitive parts of the relevant area from supra-competitive prices."[98]

Qwest further argues that a more granular market definition is not necessary to protect competition for individual routes because competitive special access providers "can often invoke Section 251(c)(3) to purchase unbundled network elements to serve those routes—and that option essentially equalizes the potential for competition across the entire MSA."[99] While the Commission already rejected the notion that UNEs were not sunk investments that could protect competition when the *Pricing Flexibility Order* was adopted,[100] UNEs were then widely available with few limitations. As explained above, this is no longer the case and therefore, UNEs cannot be relied on as a possible safeguard to force special access rates to competitive levels if real competition does not exist or materialize.

AT&T also argues that narrowing from a MSA approach to a building-by building approach would be "burdensome and unworkable."[101] Qwest likewise argues that the Commission previously rejected a more granular wire center test in the *Pricing Flexibility Order* because of administrative burdens and should do so again.[102] Contrary to these claims, compelling record evidence demonstrates that because the BOCs have enormous monopoly

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[97] *Id*.

[98] *Id*. at 33.

[99] Qwest 1/19/10 Comments, at 30.

[100] *Pricing Flexibility Order*, ¶ 94 (explaining that "UNEs do not represent sunk investment in facilities used to compete with incumbent LECs in the provision of special access and dedicated transport services, and so we reject Bell Atlantic's proposal that we include purchase of UNEs as a measure of competitive presence within a wire center.")

[101] AT&T 1/19/10 Comments, at 46.

[102] Qwest 1/19/10 Comments, at 29.

power in MSAs where they have obtained pricing flexibility,[103] the MSA is an inappropriate geographic area to grant pricing flexibility. The Commission's previous adoption of the triggers does not justify sustaining them again in the face of this evidence. Indeed, when the Commission adopted the triggers in the *Pricing Flexibility Order*, it did so in the belief that the triggers were "sufficient to ensure that competitors have made sufficient sunk investment within an MSA"[104] and "incumbent LECs cannot exercise any remaining monopoly power indefinitely,"[105] which has not been the case. As Commenters have shown, the Commission can accomplish a building-by-building or route-by-route analysis with administrative ease.[106]

AT&T further contends that a building-by-building approach would not account for potential competition.[107] It maintains that "by the time the ILEC could get pricing flexibility for the building, the competitor would likely already be serving the customer."[108] It is ironic that AT&T asserts customers do not wait for a regulatory process when they need service, because by the same token, customers do not wait for competitive carriers not already serving a building to construct and deploy facilities to the building and for that reason, potential competition should not be considered.

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[103] *See, e.g.*, PAETEC *et al.* 1/19/10 Comments, at 18-21.

[104] *Pricing Flexibility Order*, ¶ 74.

[105] *Id*. ¶ 144.

[106] PAETEC *et al.* Comments, at 57-59; *see id*. at 35 (if the Commission determines that analyzing the channel termination market on a building-by-building basis is not administrable, aggregating on a wire center level is far more preferable than aggregating on an MSA level).

[107] AT&T 1/19/10 Comments, at 46.

[108] *Id*. at 46.

While AT&T argues that wire centers or rate centers may be alternatives, it admits wire centers are "guaranteed to be inaccurate in very substantial ways."[109] AT&T asserts that there is no basis to assume a the existence of a competitor with collocation facilities in a central office will only compete within the wire center where that office is located and that CLECs may not even be collocated or be collocated in carrier hotels.[110] Despite AT&T's argument that a wire center or rate center approach to determining pricing flexibility would not reflect the "realities" of how special access competition actually occurs, AT&T's arguments demonstrate that assessing competition that exists to a particular building or on a given route cannot be based on whether carriers are collocated in a wire center but rather whether competitors are offering facilities-based services to a particular building (or location in a building) or on a given route.

B. What Analytical Framework Should the Commission Apply so that the Pricing Flexibility Rules Ensure Just and Reasonable Rates?

1. The Commission Should Apply its Traditional Market Power Analysis to Determine Where Competition Exists and Where Some Pricing Flexibility May be Warranted

Verizon and AT&T mount a broad array of arguments why the Commission should avoid conducting the intensive data driven market power analysis advocated by special access competitors and customers. AT&T contends that the Commission is bound by its 1999 decision to adopt a collocation based test and eschew the rigor of a market power test.[111] Verizon, in a classic case of putting the cart before the horse, argues that because the marketplace is purportedly "competitive," no market power analysis is necessary.[112] Verizon concedes,

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[109] AT&T 1/19/10 Comments, at 46.

[110] *Id*. at 47.

[111] AT&T 1/19/10 Comments, at 24.

[112] *See* Verizon 1/19/10 Comments, at 5.

however, that "the FCC can evaluate the efficacy of its current price cap and pricing flexibility rules by assessing the competition that has developed under the existing regulatory regime."[113] Verizon then proposes to short circuit the kind of rigorous market analysis Commenters proposed in their initial comments, claiming that "none of the indicia of market power" exist in the special access market — but without actually allowing the Commission to put Verizon's hypothesis to the test. The Commission has made it clear in the context of its investigation into broadband issues that making policy decisions based on assertions or anecdotal claims rather than hard data is not the right way to proceed.

Verizon and AT&T's claims are, however, undermined by Qwest's sensible call for a more nuanced market power analysis.[114] Special access customers, such as Sprint, also propose a similar market-power based analysis.[115] In conducting this test, however, the Commission cannot ignore current market realities — for example ignoring market share as Qwest and the other BOCs propose — and focus solely on "potential" competition.[116] In advocating a potential competition framework, the BOCs conveniently ignore the reality that a pricing flexibility regime that overemphasizes potential competition, while eschewing an analysis of actual market conditions, is nothing more than the existing pricing flexibility regime that is a proven failure.

In their Initial Comments, the Commenters urged the Commission to adopt an analytical framework similar to the Commission's "traditional market power analysis" that focuses on (a) "identifying the relevant product and geographic markets;" (b) "identifying the market

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[113] Verizon 1/19/10 Comments, at 5.

[114] Qwest 1/19/10 Comments, at 31.

[115] *See* Sprint 1/19/10 Comments, at 7.

[116] *See* AT&T 1/19/10 Comments, at 23-25; Verizon 1/19/10 Comments, at 29-30.

participants" (c) assessing the shares of market participants and the elasticities of supply and demand, and (d) determining whether the incumbent retains market power.[117] Nothing in the BOC comments should dissuade the Commission from employing this time-tested analytical approach that looks primarily to existing competition and does not permit vague and ambiguous predictions of future competition from fringe technologies to outweigh facts regarding current competitive conditions.

a. A pricing flexibility regime that fails to consider current market share can not accurately assess the extent of special access competition

The BOCs contend that the Commission's analytical framework should eschew an analysis of current market share, despite the Commission's established precedent that incorporates a market share analysis - in addition to other factors, into a market power analysis.[118] It is of course, in the BOCs' interest for the Commission to forego a rigorous market analysis because it is inevitable that the result will confirm the conclusions of the GAO and NRRI studies showing that the BOCs retain enormous market power and that the pricing flexibility regime allows the BOCs to expand that market power instead of fostering competition.[119] The BOCs raise numerous objections to the Commission's use of market share as a component of its special access analytical framework, none of which the Commission should give any serious weight.

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[117] *See* PAETEC *et al.* 1/19/10 Comments, at 28 (citing *Comsat Non-Dominance Order*, 13 FCC Rcd at 14098 ¶ 24).

[118] *See Comsat Non-Dominance Order*, 13 FCC Rcd at 14098 ¶ 24; *Dominant/Non-Dominant Order*, 12 FCC Rcd at 15766.

[119] *See, e.g.*, Sprint 1/19/10 Comments, at 17 (arguing that NRRI and GAO show the BOCS retain "an overwhelming share of the special access" market and that customers and competitors "remain highly reliant on incumbent LECs for special access").

First, the BOCs claim that the Commission may not use market share alone to judge whether a special access market is competitive. Of course, none of the commenters in the proceeding propose a *per se* market share test.[120] The Initial Comments filed by Commenters specifically observe that the Commission "has never viewed market share as an essential factor,"[121] even though years of antitrust jurisprudence suggest that market share alone can establish the existence of a monopoly.[122] Consistent with Commission precedent, Commenters have suggested that the Commission use market share as one piece of evidence to consider in evaluating the competiveness of a particular market.[123] Like Commenters, others favoring a market based analysis have suggested that, consistent with Commission precedent, the special access analytical framework should consider market share along with other factors, such as supply elasticity, demand elasticity and barriers to entry.[124]

Second, the BOCs repeatedly use the term "dynamic" to characterize the special access market, in the apparent belief that if a market is "dynamic," it need not be subject to a rigorous analysis.[125] But the BOCs never explain what factors make a market "dynamic." If this simply means the special access market is growing, the Commission has previously applied its market

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[120] *See, e.g.,* PAETEC *et. al.* 1/19/10 Comments at 27; Sprint 1/19/10 Comments at 7, Qwest 1/19/10 Comments, at 31.

[121] *AT&T v. FCC*, 236 F.3d 729, 736 (D.C. Cir. 2001).

[122] *See United States v. Grinnell Corp.*, 384 U.S. 563, 571 (1966) ("holding that the existence of monopoly "power ordinarily may be inferred from the predominant share of the market" and that the fact that one participant in the market held a market share of 87% left "no doubt" that it possessed "monopoly power.").

[123] *See* PAETEC *et al.* 1/19/10 Comments, at 27.

[124] *See id.*; *see also* Sprint 1/19/10 Comments at 7, Qwest 1/19/10 Comments, at 31.

[125] See Verizon 1/19/10 Comments, at 10.

power analysis in growing markets.[126] In the *Dominant/Non-Dominant Order*, the Commission specifically rejected the argument that characterization of a market as "dynamic" meant that less precision is needed in defining the relevant markets. To the contrary, the Commission concluded there that the "dynamic changes taking place in the long distance market place" required "more detailed market definitions … needed to assess market power accurately."[127] Likewise the markets at issue in the Commission's *Comsat Non-Dominance Order* were characterized as experiencing "unprecedented growth," yet the Commission applied its traditional market power analysis to determine those Comsat markets that were competitive and those that were not.[128] Thus, the dynamic nature of the market warranted a more searching market power inquiry rather than the cursory examination or complete disregard of those facts favored by the BOCs here.

Third, the BOCs urge the Commission to adopt a forward-looking analytical framework that captures "recent competitive activities."[129] But the BOCs do not in any way explain what this means and how this differs from an analysis of the current market, including whether price competition has eaten way at the BOCs' dominant position in special access markets. Nor do the BOCs, in advocating a forward-looking analysis, explain their inconsistent call for the Commission to examine "recent competitive activities" (which look to the past) but not adopt other modes of analysis (such as examining market share) that they paint as "backward" looking or "static."

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[126] *See Comsat Non-Dominance Order*,13 FCC Rcd at 14098 ¶ 24 (satellite markets); *Dominant/Non-Dominant Order*, 12 FCC Rcd at 15766 (interexchange markets).

[127] *Dominant/Non-Dominant Order*, 12 FCC Rcd at 15776-77 ¶ 30.

[128] *Comsat Non-Dominance Order*, 13 FCC Rcd at 14096 ¶ 19.

[129] Verizon 1/19/10 Comments, at 10.

Similarly, the BOCs claim that competitors are poised to deploy new facilities and take market share from the BOCs, particularly as demand for higher capacity special access facilities increases, citing the needs of wireless carriers for fiber-based backhaul as an example.[130] They therefore ask the Commission to incorporate competitor and customer planning information into its analytical framework. But the BOCs' proposal cannot be taken seriously — how far in advance must the Commission go when it looks into its crystal ball to determine where competitive facilities will be deployed in the future? While the BOCs have successfully played this card before, the facts from the last several years show that relying on these types of plans as evidence of competition that will constrain the BOCs is a fool's errand. In the early 2000s, the BOCs touted broadband over power lines as the new coming of intermodal competition that would act as a check. Then plans for citywide WiMAX were touted as the next source of potential competition that justified deregulation for the BOCs. These plans simply did not materialize. As the pricing flexibility regime demonstrates, deregulation — even of the limited type afforded the ILECs under the Commission's pricing flexibility rules based solely on unverifiable claims about potential competition — is doomed to fail. As tw telecom explains, "the many relevant economic and operational barriers which vary substantially by location or aggregated geographic area make it very difficult to establish a single proxy test to determine the circumstances in which competitors could deploy loop facilities in the future."[131]

Fourth, the BOCs claim that the Commission should not conduct a market share analysis because it is "a time consuming process" and that "historical market information" is not

[130] *See, e.g.,* Verizon 1/19/10 Comments, at 36.

[131] TWTC 1/19/10 Comments, at 16.

useful.[132] Avoiding a rational assessment of the state of a current market when evidence suggests that the current regulatory regime has failed would appear to be arbitrary. The Commission should not forego such an analysis at this critical juncture simply because the process may be time consuming. The BOCs' advocacy shows that they are less concerned with the time the process will take and than that the analysis will validate the claims competitors and customers have long made regarding the failure of the pricing flexibility regime.

Fifth, the BOCs argue that the fact that pricing flexibility does not relieve the BOCs of dominant carrier regulation entirely is justification for failing to conduct the analysis in the first place.[133] This makes no sense. While the Commenters do not dispute that the Commission has used its traditional market power analysis to address whether a carrier or class of carriers no longer should be regulated as a dominant carrier, this does not diminish the value of subjecting the special access market to a rigorous market power evaluation. While the analytical framework may be similar, the Commission is free to adopt different thresholds for granting relief, using, for example a higher threshold to grant relief from dominant carrier regulation and a lower threshold here where the issue is pricing flexibility within a dominant carrier tariffing regime. And the BOCs' claims regarding the use of a market power framework in a dominance/non-dominance analysis underscores the need to revaluate the "broadband" forbearance granted to the BOCs' Ethernet, OCn and ATM special access services in the 2006-2007 timeframe, as proposed in Commenters' Initial Comments.[134] These decisions effectively granted the BOCs nondominant status for these services without ever conducting a meaningful and rigorous competitive

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[132] Verizon 1/19/10 Comments, at 29.

[133] *See* AT&T 1/19/10 Comments, at 25-26.

[134] PAETEC *et al.* 1/19/10 Comments, at 36-41.

assessment. The Commission should remedy that defect by conducting such an analysis in this review. Given the importance of special access to America's digital economy, the Commission's pricing flexibility regime should not be evaluated simply by subscription to vague and unsubstantiated predictions of potential competition that are not rooted in a reliable analysis that identifies where competition to date has succeeded at loosening the BOCs' grip on the special access market.

b. Each point-to-point connection is a separate geographic market

While most commenters agree that "each point-to-point connection is a separate geographic market,"[135] the BOCs vigorously dispute proposals to adopt a route-specific analysis for transport and building specific test for loops. Verizon claims that a building-by-building test does "not reflect how competitors offer their services."[136] That, however, is not the inquiry; rather, the Commission's focus should be on whether special access customers have choices — or whether are they locked into the ILEC's service without a choice of a competitive provider. This is consistent with the Commission precedent that "Commission makes its assessment of the appropriate product markets "from the perspective of customer demand."[137]

A special access customer does not care that a carrier has a fiber ring located miles away in a remote corner of the MSA. What matters is whether that competitor can offer service that competes with the ubiquitous network the ILEC has at its disposal. This requires a nuanced and more granular analysis then examining competitive conditions across an MSA. To the extent that the Commission determines it needs to aggregate its consideration of point-to-point routes it

[135] TWTC 1/19/10 Comments, at 13.

[136] Verizon 1/19/10 Comments, at 30.

[137] *SBC/AT&T Merger Order*, ¶ 83.

should "strive to keep its analysis as granular as possible, since a greater degree of aggregation necessarily entails a greater risk of misclassification of individual point-to point connections."[138]

c. The Commission's product market definition should exclude niche technologies that are not a substitutes for a sufficient percentage of special access customers

In their Initial Comments, Commenters proposed that the Commission apply the traditional market power based determination of appropriate product markets and only consider substitutes that widely viewed as substitutes for ILEC special access services.[139] The BOCs tout the potential of intermodal competition such as cable networks and fixed wireless to compete with ILEC special access services.[140] The BOCs' statements do not make it so. To the extent that cable companies actually deploy fiber based services that compete with the ILEC special access, those offerings should be considered. But the BOCs seek to water down the Commission's market power analysis by including cable company services that are not substitutes for wireline special access services, such as cable modem based services. Under long standing Commission precedent, the relevant inquiry for defining a product market is whether a sufficient number of customers would switch to a product in the face of a significant price increase by the dominant provider.[141] The fact that a limited number of customers view a product as a substitute does not necessarily mean that a *sufficient* number of customers in a market would switch to that product in the face of anti-competitive pricing or terms.

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[138] Sprint 1/19/10 Comments, at 10. As they argued in their Initial Comments **(**PAETEC *et al.* Comments, at 35), if the Commission determines that analyzing the channel termination market on a building-by-building basis is not administrable, aggregating on a wire center level is far preferable to aggregating on an MSA level.

[139] PAETEC *et al.* 1/19/10 Comments, at 31.

[140] AT&T 1/19/10 Comments, at 32-34; Verizon 1/19/10 Comments, at 20-25.

[141] *See Echostar*, ¶ 97, 106; *see also* Horizontal Merger Guidelines, §§ 1.11, 1.12.

Both cable modem based services and fixed wireless have inherent deficiencies which render them as ineffective substitutes for a broad population of special access customers, but might have appeal to a limited subset of special access customers.[142] For instance, fixed wireless service is not a viable substitute for wireline special access services for the vast majority of special access demand because of a variety of factors, including the following factors identified by Sprint:

> propagation issues that limit the distance a fixed wireless connection can cover; line of sight requirements which render fixed wireless services ineffective in certain locations; sensitivity to weather, which can affect reliability; costs that are too high to justify use for relatively low capacity connections; limited access to rooftops and other building access issues; and fixed wireless providers' focus on the retail market.[143]

Even Verizon Wireless understands the limitations of fixed wireless as a substitute for wireline special access in the backhaul market, conceding that the fixed wireless connection would be the "the most unstable part of [the] system and what limits [the wireless carrier's] bandwidth as well.""[144] Further, the shared nature of both fixed wireless systems and cable-modem based services and the issues fixed wireless technology has with reliability and service guarantees "indicates a sufficient number of customers would not shift to these intermodal alternatives."[145]

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[142] *See, e.g.,* Sprint 1/19/10 Comments, at 19-20.

[143] Sprint 1/19/10 Comments, at 19-20.

[144] Tom Swanobori, VP of Network and Technology Strategy, Verizon Wireless, at FCC Workshop on Wireless Broadband Deployment - General (Aug. 12, 2009), transcript at 48.

[145] TWTC 1/19/10 Comments, at 11.

d. The Commission should reject the BOCs' arguments that their ubiquitously deployed fiber networks do not provide them with an inherent advantage in the market for packet-based special access services, including Ethernet

The BOCs assert that the Commission's analytical framework should account for the purported fact that incumbent carriers have no advantage over competitors in providing packet-based services.[146] They further claim that incumbents have "no inherent advantage" in providing these services as they must upgrade or replace their existing facilities while Competitors must deploy new facilities.[147] Contrary to the BOCs' arguments, they do have a substantial inherent advantage over CLECs in providing packet-based services.

While both ILECs and CLECs generally need to upgrade their networks to provide packet-based services, the tasks faced by an ILEC are far less extensive than those faced by a CLEC. For an ILEC to upgrade the network it currently uses to provide existing special access services for packet-based services such as Ethernet, it simply has to upgrade the electronics. In most cases, it does not need to deploy new fiber loop facilities for the entire distance from the serving wire center to every commercial building when upgrading to packet-based technology. Because for the most part it has fiber facilities already in place deep into its local area network, it would require limited additional fiber. In addition, the ILEC can use existing hybrid fiber/copper facilities already in place to buildings and overlay its packet based electronics on the network, as long as the copper portion is relatively short.[148] In contrast, CLECs typically lack the substantial embedded facilities already possessed by an ILEC and therefore

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[146] *See e.g.* Verizon 1/19/10 Comments, at 16.

[147] Verizon 1/19/10 Comments, at 16.

[148] *See, e.g., TRO*, ¶ 285 (recognizing that ILECs modify theri networks incrementally, deploying fiber feedeer and xDSL capability before deploying fiber all the way to the custoemr premises.).

face prohibitive costs and burdens associated with deploying last mile infrastructure across a large part of the network to each customer. [149] In fact, the barriers hindering competitors from deploying their own facilities to provide Ethernet services are similar to those they face in deploying facilities to provide TDM-based special access.[150]

While the BOCs express general aversion to conducting a market power analysis, they raise no credible objections to evaluating competition in discrete product markets based on capacity levels. For instance, Verizon claims that it would make little sense for the Commission to adopt an "analytical framework to define static product markets … according to bandwidth or speed."[151] While Verizon claims that a 100 Mbps Ethernet circuit in the future may be a substitute for 2 DS3s, there can be no argument that it is not in the same product market as a DS1 or even 5-10 Mbps Ethernet circuit.[152]

The BOCs further claim that the exercise of developing a coherent analytical framework to asses the level of competition in special access markets is a waste of time because DS1 and DS3 services are going the way of the dodo.[153] Apart from the fact that DS1 and DS3 services are plainly important today and at least in the near future, this ignores the fundamental fact that that the same fiber facilities that the BOCs use to provide DS3 services can — and do — provide Ethernet services. Both require fiber. As Sprint explains, while

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[149] *See, e.g.*, Comments of Covad Communications Company, WC Docket No. 09-223, Attachment A: VIABILITY OF BROADBAND COMPETITION IN BUSINESS MARKETS, An Analysis of Broadband Network Unbundling Policies and CLEC Broadband Competition, at 5-7 & 33-36 (filed Jan. 22, 2010).

[150] *See* Sprint 1/19/10 Comments, at 21.

[151] Verizon 1/19/10 Comments, at 17.

[152] *See, e.g.*, Sprint 1/19/10 Comments, at 15 (DS1 and DS3 circuits should be in separate product markets).

[153] AT&T 1/19/10 Comments, at 2-3.

> Ethernet services are very attractive from an engineering standpoint … the economics of providing an Ethernet connection are very similar to the economics of providing a TDM-based special access connection, so that competitive carriers are no more economically able to build their own facilities to provide Ethernet services than they are to provide TDM-based special access.[154]

And AT&T's disparagement of its legacy copper plant ignores its own plans to utilize that copper to provide mid-band Ethernet.[155] The BOCs' ability to leverage their existing and ubiquitously deployed infrastructure to provide new services provides significant advantage over competitors that would have to deploy new networks to compete for customers the BOCS already serve. Nowhere is this more evident than in serving the wireless backhaul market. A significant percentage of wireless carrier cell sites are located at remote sites and the only available facility is that deployed by the BOC.[156] And while wireless carrier backhaul capacity needs are growing, the wireless carriers do not immediately need fiber. A BOC's ability to leverage that existing copper infrastructure and provide xDSL or Ethernet to cell sites, while at the same time deploying the fiber it will eventually need, provides an advantage that is hard for competitors to overcome.[157]

It is a fallacy that ILECs "have no advantage over competitors in providing these higher capacity services" because "the higher bandwidth services that customers are demanding require either upgrades to existing incumbent facilities or the construction of entirely new network

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[154] Sprint 1/19/10 Comments, at 21 n.66.

[155] "AT&T Sets Copper Ethernet Course, Craig Matsumoto, Light Reading, march 13, 2007, available at http://www.lightreading.com/document.asp?docid=119284.

[156] *See, e.g.*, Sprint 1/19/10 Comments, at 16 ("A large number of CMRS providers' cell sites are located in, and throughout, the lower-density areas of an MSA.").

[157] *See, e.g.*, Marcus Weldon, Chief Technical Officer, Wireline Networks Product Division, Alcatel-Lucent, FCC National Broadband Plan Workshop, *Deployment-Wired*, Transcript at 38 (Aug. 12, 2009).

facilities." as Verizon argues.[158] This claim ignores the fundamental fact that for most special access locations, including wireless carrier cell sites, the BOC is the only provider with existing in-place facilities at or near the cell site and already has substantial network infrastructure that can be upgraded or replaced more easily than a new entrant can deploy a new network to serve that customer.[159] The BOCs also fail to acknowledge that their vast integrated businesses, including their wireless and interexchange businesses, provide them vast advantages in economies of scale and scope. As Sprint observes, by "transporting traffic of multiple services on the same facilities, the incumbent LEC is able to support the cost of those transport facilities with revenues from multiple services - an advantage that new entrants lacking the vertical integration advantages of AT&T and Verizon are unlikely to possess."[160]

[158] Verizon 1/19/10 Comments, at 16.

[159] Sprint 8/8/07 Comments, Attachment 1: Declaration of Gary B. Lindsey, ¶ 5 (competitors could reach approximately 1 percent of Sprint's 52,000 cell sites for which it sought competitive alternatives.).

[160] Sprint 1/19/10 Comments, at 24.

e. The BOCs' proposal to collect information on potential deployment projects will unnecessarily complicate the data collection process and increase the burden on carriers with little to no added public benefit.

In addition to arguing that the Commission's analytical framework should emphasize potential competition and ignore actual competition, the BOCs further ask the Commission to collect detailed data from special access competitors and customers regarding this purported "potential competition." The Commission should reject this data collection proposal as the data sought is simply not reliable, the burdens such a collection imposes are unreasonable, and as the existing pricing flexibility regime demonstrates, potential competition does not discipline the BOCs' special access pricing.

The unreasonableness of the BOCs' data collection proposal is illustrated by Verizon's proposal that the Commission ask special access customers for information about their ability and plans to self supply high capacity services.[161] First, it is unclear what authority the Commission would have over purchasers of special access that are not themselves carriers subject to Commission jurisdiction.[162] In addition to being unreliable in comparison to evidence of existing competition and supply, there is no reliable evidence to support the contention that customer self supply is a viable constraint on anticompetitive pricing of ILEC special access services.

In their effort to promote a special access analysis that avoids an evaluation of the significant market shares the BOCs continue to enjoy as a legacy of the historical monopolies,

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[161] Verizon 1/19/10 Comments, at 38.

[162] *See generally American Library Ass'n v. FCC*, 406 F.3d 689 (D.C. Cir. 2005) (FCC's general grant of authority over communication by wire or radio did not provide FCC authority to regulate apparatus that merely received communication content.).

the BOCs also ask the Commission to collect a broad array of data regarding "planned" network facilities of all competitors that are operating or are planning to operate in the relevant geographic market.[163] For example, AT&T suggests that the Commission seek information on carriers' "current plans to upgrade and expand existing networks (or build new ones) to additional buildings and geographic areas and to deploy new services."[164] The BOCs then expect the Commission to 'predict" where future network expansions will occur and to use these "predictions" to formulate policy.[165]

But this could be a never ending, open-ended inquiry depending on the level of specificity the Commission sought and what activities would constitute "plans." If a carrier's long-term business plan calls for deploying facilities in a market in three years, but the carrier has not budgeted for the capital expenditure and has not contracted for its construction does that qualify as a plan that must be provided to the Commission? It could take years for the Commission simply to develop the guidelines necessary to distinguish between those deployment plans that need to be collected and those that do not.

The Commission should reject the BOCs' overbroad, intrusive and wasteful data collection proposals, associated with potential competition (this includes AT&T's request for RFPs, unsolicited proposals to prospective customers, deployment feasibility studies and network upgrade plans) along with data associated with wireless or other services that are not currently substitutes to the BOCs' special access services. None of this data collection will assist the Commission with assessing where and how much competition exists for the incumbent's

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[163] *See, e.g.,* Verizon 1/19/10 Comments, at 34.

[164] *See* AT&T 1/19/10 Comments, at 42.

[165] *See, e.g.,* Verizon 1/19/10 Comments, at 35-36.

special access services. Qwest on the other hand, consistent with the Commenters' Initial Comments, asserts that the Commission should compile all data needed to conduct a genuine market-power analysis for the relevant markets and observes that the Commission is no stranger to such a market-power analysis, given the central role of these types of analysis have played in recent merger, nondominance, and forbearance proceedings.[166] The Commenters' proposal to require all providers (competitors and incumbents), to submit data about lit on-net buildings is far more reasonable than the AT&T and Verizon proposals.[167]

Nor should the Commission accept Verizon's invitation to exclude rate zone 1 areas in the Top 50 MSAs based on its assertion that such areas are competitive.[168] Verizon's assumption that Zone 1 areas are competitive is contradicted by market experience. As discussed in Commenters' Initial Comments, the pricing flexibility triggers are flawed and zone 1 regions are no exception to the overwhelming evidence that where BOCs have obtained phase II pricing flexibility, they continue to exert significant market power to the detriment of competition and customers. At bottom, the Commenters' proposed approach to gathering information should be adopted over the approach proposed by Verizon.

(2) Do The Price Cap Rules Ensure Just And Reasonable Rates?

As Commenters previously demonstrated, the Commission's price cap rules do not ensure the just and reasonable rates that Section 201(b) of the Act requires.[169] The Commission made clear in implementing the price cap regime that observed returns remain the litmus test for determining whether the specific price cap rules are working to protect consumers from unjust

[166] *See* Qwest 1/19/10 Comments, at 31.

[167] PAETEC *et al.* 1/19/10 Comments, at 54-56.

[168] *See* Verizon 1/19/10 Comments, at 42.

[169] *See* 47 U.S.C. § 201(b).

and unreasonable rates. The Commission expressly stated that a "price cap approach cannot free carriers to earn excessive [supracompetitive] profits in light of their costs."[170] It further acknowledged that its price cap regime would include "ongoing monitoring" and that a future "comprehensive review" of the price cap mechanism would "focus prominently on the carrier costs and profits."[171] As explained below, the Commission should reject the BOCs' claims that the Commission should not so focus, as well as their criticisms of ARMIS data and proposed pricing/costing benchmarks. The Commission should adopt the proposed measures and reforms to the price cap rules the Commenters proposed.

A. The Commission Should Evaluate the BOCs' Costs and Profits

The BOCs argue that the Commission should not undertake an analysis of costs and profits in determining whether price cap rates are reasonable because doing so would be unnecessary or inappropriate.[172] They generally argue that Commission should not consider costs and profits because (1) prices have assertedly fallen;[173] (2) it would not be practical or feasible for the Commission to measure or calculate them;[174] and/or (3) doing so would be contrary to price cap regulation and the efficiency incentives associated therewith.[175]

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[170] *Policy and Rules Concerning Rates for Dominant Carriers, Report and Order and Second Further Notice of Proposed Rulemaking*, 4 FCC Rcd 2873, ¶ 885 (1989).

[171] *Id*.

[172] *See, e.g.,* AT&T 1/19/10 Comments at 10, 49-69; Verizon 1/19/10 Comments, at 43-48; Qwest 1/19/10 Comments at 44-49.

[173] *See, e.g.,* Verizon 1/19/10 Comments, at 43.

[174] *See, e.g.,* Verizon 1/19/10 Comments, at 43-44; AT&T 1/19/10 Comments, at 61-62; Qwest 1/19/10 Comments, at 22.

[175] *See, e.g.,* Verizon 1/19/10 Comments at 43-44; AT&T 1/19/10 Comments at 50 & 63; Qwest 1/19/10 Comments at 48. AT&T asserts "These incentives for increased efficiency, investment, and innovation would not exist, however, unless the ILECs could keep the increased profits that these improvements in efficiency make possible." AT&T 1/19/10 Comments, at 52.

Contrary to the BOCs' claims, as shown in Section II.(1), the record evidence shows that actual rates have not fallen and price cap rates are otherwise at unreasonable levels for the reasons the Commenters previously discussed.[176] Nor would it be impractical, infeasible, or arbitrary for the Commission to analyze special access costs and profits for ILECs currently subject to price cap regulation because the Commission already does so for ILECs that are subject to rate-of-return regulation.[177] Price cap ILECs should not be permitted to avoid a rate-of return audit when evidence indicates their returns are excessive and rate-of return carriers continue to be subject to such regulation. For far too long, BOCs have exploited the special access price cap rules by overcharging competitors and end users alike for special access services, thereby allowing the BOCs to earn supracompetitive profits.

AT&T argues that it would take numerous man hours to determine what portion of the network should be allocated to special access services.[178] Even if AT&T's estimate (which is likely a dramatic embellishment) were correct, these man hours pale in comparison to the 234,000 jobs and $66 billion in economic output the BOCs' overcharges cost the U.S. economy

[176] PAETEC *et al.* 1/19/10 Comments, at 59-80.

[177] AT&T and Verizon submit that because special access services are provided almost entirely over the same transport and loop facilities that are used to provide a full range of ILEC services, it would be arbitrary to determine the joint and common costs of special access services. AT&T 1/19/10 Comments, at 62; Verizon 1/19/10 Comments, at 43. Contrary to AT&T and Verizon's claims, the "telephone network …has always been comprised of extensive amounts of joint and common plant that were – and are – used to support the provision of multiple and different services to individual customers, requiring a cost allocation exercise to set prices." Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 10.

[178] AT&T 1/19/10 Comments, at 49.

for the three year period from 2007 to 2009 alone.[179] In short, the Commission continues to look at costs and revenues for rate-of-return carriers to ensure they are not over-earning and given the strong evidence in the record that BOCs are over-earning on special access to a significant degree, can and should take the same approach with the BOCs.

As to the BOCs' arguments that evaluating a price cap carrier's profits and costs would undermine price cap efficiency incentives, such arguments have no merit. While the Commission had hoped that competition would discipline the BOCs' special access prices and drive those prices to competitive, forward-looking levels, that did not happen.[180] The Commission did not adopt price caps to permit price cap ILECs to assess unjust and unreasonable rates. Indeed, as noted above, the Commission warned price cap ILECs that a future "comprehensive review" of the price cap mechanism that "focus[es] prominently on the carrier costs and profits" was inevitable.[181] The Commission further acknowledged this in the

[179] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at i.

[180] AT&T argues that the Commission previously rejected nearly identical calls to reinitialize price caps based on rates of return in 1997 and explained at length there why such measures "would destroy the benefits of price cap regulation." AT&T 1/19/10 Comments, at 54. In contrast with the record in 1997, the record now includes various other benchmarks, apart from rate-of-return data, that demonstrates that BOCs' special access rates are patently unreasonable. The Commission cannot ignore this compelling evidence and condone the BOCs' continuing violation of Section 201(b) of the Act.

[181] Contrary to the BOCs' contentions, the Commission's price cap rules can be modified or repealed altogether. *Ad Hoc v. FCC*, No. 07-142, *slip op.* at 16 (D.C. Cir. 2009) (explaining that the FCC's "decision in [a] particular matter… is not chiseled in marble" and can be reassessed as it reasonably sees fit "based on changes in market conditions, technical capabilities, or policy approaches to regulation in this area."). The D.C. Circuit recently recognized that the FCC has every right to change course and revise its decision as long as it provides a reasoned basis for doing so. *Verizon Tel. Cos. v. FCC*, No. 08-1012, *slip op.* at 12 (D.C. Cir. June 19, 2009) (citing and quoting *Motor Vehicle Mfrs. Ass'n, Inc. v. State*, 463 U.S. 29, 57 (1983) and stating if the

Public Notice itself by stating, "We would expect any analytical framework, based on ARMIS or not, to include specifics as to the measure of profit and the reasonableness of that profit."[182] Further, the Commission could, as Commenters propose, reinitialize price cap rates so that they are set at reasonable levels and impose modified price cap rules to apply that provide efficiency incentives to the extent the original 1991 price cap rules contemplated. In any event, for the reasons set forth in Sections I(2) and (3) above, the BOCs have an obligation to provide, upon request by the Commission, all accounting cost and revenue data that the Commission requires to determine if the BOCs are violating Section 201b) of the Act and improperly subsidizing non-regulated services with regulated services in violation of 254(k) of the Act. The Commission should accordingly request that the BOCs produce this accounting data.

B. ARMIS Data Provides Substantial Evidence that the BOCs are Exercising Market Power Over Special Access Services and Obtaining Increasingly Supracompetitive Profits and Returns

As demonstrated in earlier comments, the BOCs' extraordinarily high special access rates-of-return that ARMIS data reveals clearly show that the Commission's regulatory framework governing special access pricing is not producing just and reasonable rates and that BOCs retain market power over special access services.[183] Similar to their arguments in 2005 and 2007, the BOCs again assert that ARMIS rate-of-return data is flawed and unreliable, and

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FCC changes course, it "must supply a reasoned analysis" establishing that prior policies and standards are being deliberately changed) (external quotation omitted)).

[182] *Parties Asked to Comment on Analytical Framework Necessary to Resolve Issues in the Special Access NPRM*, Public Notice, WC Docket No. 05-25, RM-10593, DA 09-2388, at 5 (rel. Nov. 5, 2009)

[183] PAETEC *et al.* Comments, at 64-67; ATX *et al.* 8/8/07 Comments, at 11-15; ATX *et al.* 7/29/05 Comments, at 10-14; ATX *et al.* 6/13/05 Comments, at 7-10.

should not be used to assess their market power or for ratemaking purposes.[184] For the reasons explained below and as the record fully demonstrates,[185] these criticisms can be readily rejected.

First, the BOCs argue that the ARMIS cost and accounting data are based on arcane and arbitrary allocations associated with jurisdictional separations, common costs, and divisions between regulated and unregulated services.[186] Contrary to these assertions, the allocations and the cost and revenue data they report to the Commission through ARMIS are neither arcane nor arbitrary.[187] ARMIS "is 'regulatory' accounting data developed according to a strict set of

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[184] *See* AT&T 1/19/09 Comments, at 67-72; Qwest 1/19/10 Comments, at 44-46; Verizon 1/19/10 Comments, at 45-48.

[185] *See, e.g.,* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS; Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-1 though A-13; ETI 2004 Report, at 27-35; PAETEC *et al.* Comments at 64-67; ATX *et al.* 8/8/07 Comments, at 11-15; ATX *et al.* 7/29/05 Comments, at 10-14; ATX *et al.* 6/13/05 Comments, at 7-10.

[186] AT&T 1/19/10 Comments, at 61-62, 67-72; Qwest 1/19/10 Comments, at 44-45; Verizon 1/19/10 Comments, at 45-48. Verizon also argues that the Commission should ignore ARMIS rates-of-return for special access because any focus on costs would effectively revert to rate-of-return regulation. Verizon 1/19/10 Comments, at 44. Contrary to Verizon's claims and the Commission's predictive judgment, competition has failed, however, to materialize and constrain the BOCs' monopolistic pricing behavior. Consequently, the Commission is compelled to intervene and reinitialize prices for ILEC monopoly controlled services at a level that is just and reasonable and allows for a reasonable rate-of-return. The Commission has emphasized that if forward-looking prices failed to materialize, it would be compelled to reinitialize special access rates, which is rate-of-return ratemaking. *See, e.g., Access Charge Reform Order*, ¶ 48 ("Where competition has not emerged, we reserve the right to adjust rates in the future to bring them into line with forward-looking costs"). The Commission even gave price cap ILECs an option to file forward-looking cost studies, which is rate-of-return ratemaking, as required by the *Access Charge Reform Order* or make voluntary reductions contemplated under the CALLS plan; however, "[a]ll price cap carriers opted for the CALLS plan." *Special Access NPRM*, ¶ 15.

[187] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-3; *see also* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 6-26.

accounting rules established by utility accounting experts."[188] These rules are specifically designed to "differ from the 'financial' accounting data" the BOCs report to their shareholders and the SEC.[189] Ironically, if financial accounting were applied instead of regulatory accounting, the rates-of-return would likely be higher than those reported to the Commission.[190] Significantly, ARMIS reporting is done at the service category level. As a result, certain categories of cost that support multiple services, such as switched and special access services, must be allocated among the relevant services.[191] That the allocations may be less than precise does not make them useless for the purpose of regulatory analysis, which is why they were originally established.[192]

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[188] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-3.

[189] *Id*.; *see also* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 5.

[190] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-3; *see also* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 5.

[191] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-3; *see also* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 5.

[192] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-3; Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 5.

Second, the BOCs argue that ARMIS data was never used to set prices and that accounting rates of return are meaningless;[193] however, "evaluating earnings levels though analysis of regulatory accounting data *is not setting prices*."[194] Their arguments also strain credulity because the BOCs have repeatedly embraced ARMIS data when it benefits them for ratemaking purposes. As ETI has shown, the BOCs have in other contexts emphasized the tremendous value and utility of ARMIS data for ratemaking purposes.[195] Indeed, although the BOCs are quick to discredit ARMIS data when it demonstrates that they are over-earning, they are often eager to offer it to regulators to show that UNE prices are too low.[196] In any event, as discussed below, record evidence shows that even if there are any misallocations, it is more likely that costs from other ILEC services are being improperly assigned to special access and that the actual rates-of-return are higher than reflected by ARMIS data.[197]

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[193] *See* AT&T 1/19/10 Comments, at 49, 58, & 61; Verizon 1/19/10 Comments, at 46; Qwest 1/19/10 Comments, at 22 & 44. While AT&T further argues that "service-specific returns would be even more meaningless" (AT&T 1/19/10 Comments, at 60; *see also* Qwest 1/19/10 Comments at 46), yet for the reasons discussed, its arguments have not merit as AT&T has embraced ARMIS when it has benefited AT&T.

[194] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, Appendix 1 at A-3 (emphasis added).

[195] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 17-19; Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, Appendix 1 at n.41; *see also* Ad Hoc 6/13/05 Comments, at 29-31; ETI 2004 Report, at 30 & n.56.

[196] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 17-19.

[197] ETI 2004 Report, at 33; *see also* Ad Hoc 8/8/07 Comments, Declaration of Susan M. Gately, ¶ 15. ETI explained that for 2003, the new investment allocated to the special access category for the four BOCs was roughly one third of their total interstate net investment and approximately 40% of their combined Common Line and Special Access Investment categories.

Third, the BOCs continue to argue that the 2001 separations freeze of ARMIS cost categories distort any attempt to use these data to approximate special access rates-of-return.[198] There is, however, no evidence that this separations freeze has resulted in an under-allocation of expenses or investments to the special access category.[199] The BOCs basically assert that the freeze has resulted in the growth in special access demand (lines or revenues) being greater than the growth in special access investment, and that this difference in growth rates results in under-allocation of investment and expenses to the special access category.[200] This argument does not withstand scrutiny because there should be no expectation that the rates of change in special access "demand" and "investment" levels will be identical.[201] For example, if a special access customer subscribing to a single OC-3 line (2,016 VGEs) decides to purchase additional bandwidth and replaces the OC-3 with an OC-12 (8,064 VGEs), special access VGE demand

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Id. ETI noted that because there are only about 4-million special access loops and associated interoffice transport facilities, compared to more than 158-million Common Line local service loops in the BOCs' operating territories, the allocated investment is entirely disproportionate to the number of special access loops, as a percentage of total loops in service. *Id*. Thus, the wide discrepancy between the number of loops used for special access and the amount of interstate investment assigned to those loops certainly raises suspicions that costs are being over-allocated to the special access category. *Id*. 2005 data confirms this. *Id*. Other possible misallocations that could produce rates-of-return higher than reflected by ARMIS data are discussed below.

[198] Verizon 1/19/10 Comments, at 46-47; AT&T 1/19/10 Comments, at 68-69; Qwest 1/19/10 Comments, at 45.

[199] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-5 (bolding removed); *see also* Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at iv & 11-14.

[200] *See, e.g.*, Verizon 1/19/10 Comments, at 47; AT&T 1/19/10 Comments, Exhibit B: Declaration of Ron Hilyer and Thomas Makarewicz, at 10; Qwest 1/19/10 Comments, at 45.

[201] Ad Hoc 8/8/07 Comments, Appendix1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at Appendix 1 at A-5.

increases by 300%, yet an OC-12 costs only a small amount (as little as 5% to 10%) more than an OC-3.[202] Moreover, "[t]he 2001 [s]eparations 'freeze' has not stopped the proportion of total investment and expenses allocated to the [s]pecial [a]access category from increasing,[203] despite the BOCs arguments to the contrary. As the record demonstrates, special access "expense and investment dollars should not be growing as fast as revenues" because "the relative growth in demand (expressed in terms of revenues) is far greater than the relative increase in the cost required to furnish the services."[204]

In any event, even if ARMIS rates-of-return are not precise (because of the alleged misallocations noted by the BOCs),[205] the trend in the data, as shown in earlier comments, is steadily rising and is a reliable indicator of the BOCs' ability to increase prices to supracompetitive levels without fear of attracting competitive entry.[206] Moreover, despite their

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[202] *Id*. at Appendix 1 at A-5; *see also* Ad Hoc 8/8/07 Comments, Declaration of Susan M. Gately, ¶ 16 (explaining that the costs of special access services are trending down much more so than rates on a VGE equivalent basis); Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 14.

[203] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 13 (bolding removed).

[204] *Id*. at 15. AT&T further argues that "ARMIS-based figures for average net investment, the denominator in the ARMIS-based rate-of-return calculation, are likely understated, which also inflates the ARMIS-based rate of return calculations." AT&T 1/19/10 Comments, at 71. AT&T argues that third-party data estimates of ILEC plant reproduction costs have increased substantially over the period of pricing flexibility. *Id*. AT&T's estimates are likely well overstated if they improperly include reproduction costs for new broadband deployment, which should not be in the calculation as described below, and do not reflect the fact that legacy TDM technology (which special access services are provisioned over) has likely been fully depreciated and is no longer being deployed.

[205] ATX *et al.* 8/8/07 Comments, at 12-13.

[206] *Id*. at 14; Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at iii & 3-4; *see also* ETI 2004 Report, at 29-30.

criticisms about the allocations, the BOCs are still experiencing phenomenal interstate rates-of-return overall. "Average [BOC] earnings for the totality of FCC regulated interstate access services are almost three times higher than the last authorized rate of return. Interstate earnings for each RBOC ranged from a low of 25.2% (for Verizon) to a high of 53.2% (for Qwest)."[207] These returns are considerably more than double the Commission's prescribed 11.25 percent rate of return "benchmark for determining whether price cap LECs' special access rates are just and reasonable."[208] Moreover, the fact that the 11.25 percent rate of return is outdated and should likely be in the 8 to 9 percent range or lower[209] further proves that the BOCs' earnings are excessive by any standard.[210]

Fourth, if anything, the BOCs' average rates-of-return are likely significantly understated and far exceed NRRI's computation.[211] As ETI demonstrated, special access and other regulated

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[207] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 19.

[208] *Special Access NPRM*, ¶ 60.

[209] ATX *et al.* 6/13/05 Comments, at 23-24; Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 3 n.3. *see also* Ad Hoc 8/8/07 Comments, at 24-25. AT&T further argues that using 11.25 percent rate-of-return benchmark for assessing special access would be inappropriate because it was an enterprise wide rate-of-return that took into account both the ILECs' more and less competitive services. AT&T 1/19/10 Comments, at 67. AT&T's argument is flawed because it incorrectly assumes that the special access market is competitive. Therefore, AT&T's return for non-competitive special access services should not be set at levels that permit it to earn excess profits and subsidize truly competitive service offerings in contravention of Section 254(k).

[210] *See also* Ad Hoc 6/13/05 Comments, at 41-42.

[211] The NRRI Report concluded the BOCs have raised prices above average costs and show earnings well above the 11.25% authorized return that the FCC last prescribed for price cap carriers. NRRI Report at 71. AT&T asserts that with a few additional investment and expense adjustments to NRRI calculations, the NRRI return for special access service would be 24.30%, which is, as AT&T claims "no higher than the service specific returns (as calculated using ARMIS data) in 1999 when the Commission adopted the pricing flexibility rules." AT&T

services rates-of-return as reported in ARMIS are almost certainly understated because of the inclusion of BOC capital expenditures made for the purpose of offering unregulated broadband and video services, such as Verizon's FiOS and AT&T's Project Lightspeed, within the "regulated services" category.[212] Adjusting ARMIS reported special access category investment so that it excludes non-regulated broadband investments from the regulated services category would increase Verizon's and AT&T's average special access rate of return of 99% to 177%, respectively.[213]

1/19/10 Comments, at 70-71. For the reasons discussed herein, AT&T's rate-of-returns are likely significantly understated and likely approximate 177%. Moreover, the fact that AT&T was experiencing a higher than 24.30% return when the Commission's pricing flexibility rules were adopted does not mean the Commission implicitly sanctioned excessive earnings. Rather, the Commission likely implicitly expected that since Section 251(c)(3) UNEs were available to all carriers, *i.e.*, CLECs, wireless and IXCs, when the pricing flexibility rules were adopted in 1999 to perhaps discipline special access pricing. As the Commission recognizes, UNEs are no longer available for the exclusive provision of mobile wireless or interexchange services. *See* 47 C.F.R. § 51.309(b). Moreover, the *TRO* and *TRRO* dramatically reduced the types of Section 251(c)(3) UNEs that ILECs must offer to CLECs. Even those DS1 and DS3 UNEs which remain available as UNEs are no longer available everywhere to CLECs, since they are not available where certain caps or *TRRO* non-impairment thresholds are met. Given these limitations, the availability of UNEs cannot be relied on as a safeguard to force the ILECs to reduce their special access rates (and rates of return) to competitive levels.

[212] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 20-26; Ad Hoc 8/8/07 Comments, Appendix1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at 16-18 and Appendix 1 at A-8 through A-10. Verizon admits its reported special access revenues included revenues for DSL and FiOS. Verizon 1/19/10 Comments, at 9 n.15.

[213] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 25. Verizon also asserts that its 2007 total company return for regulated services was 9.5 percent and therefore its returns are well within reasonable levels in an intensely competitive telecommunications market. Verizon 1/19/10 Comments, at 48. AT&T also argues that its returns are reasonable because its total company returns have not significantly changed since the Commission adopted its pricing flexibility rules. AT&T 1/19/10 Comments, at 71. Notably, Verizon concedes that "total company profitability says nothing about the profitability of an individual service and therefore has little relevance to a competitive analysis of that service." Verizon 1/19/10 Comments, at 48.

Fifth, because TDM technology has likely been fully depreciated and Qwest's actual rates for special access services have not decreased, Qwest's analysis demonstrates that Qwest and the other BOCs are obtaining higher and higher accounting rates of return.[214] Qwest argues that accounting rates are artificial measures of net revenues that depend on factors such as depreciation and therefore, ARMIS data do not reflect some unjust increases in revenues or profitability. Contrary to Qwest's assertions, the price for competitive services should decrease over life of the competitive services; because Qwest's special access rates have not, Qwest is now experiencing excessive returns.

Finally, as Commenters explained previously, although the BOCs have argued that the Commission should not rely on ARMIS rates-of-return data, they have failed to provide any evidence demonstrating what their special access rates-of-return are under some other measure that they deem more appropriate. Indeed, as ETI explained, "the notion that the ILECs have no internal cost data specific to special access services other than the supposedly flawed ARMIS data, when special access represents some $17-billion in annual RBOC revenue, strains credulity beyond all reasonable limits."[215] Moreover, as discussed in Sections I.(2) and (3) above, in gaining forbearance from filing ARMIS data, the BOCs agreed to produce accounting data upon request so that the Commission can determine if they are complaint with Sections 201(b) and

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In any event, given AT&T's and Verizon's adjusted special access ARMIS rates-of-return, this shows that Verizon and AT&T may be subsidizing their competitive offerings with revenues from their noncompetitive offerings. Such actions are contrary to forward-looking cost-based pricing reflective of a competitive market and as discussed in Section I.(3) above, prohibited by Section 254(k) of the Act.

[214] Qwest 1/19/10 Comments, at 47 & Declaration of Timothy J. Tardiff and Dennis L. Weisman, at ¶ 25 and Table 1.

[215] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at 9.

254(k) of the Act. Therefore, the BOCs should have this cost accounting information readily available and be able to produce it upon Commission request.

For the above reasons, ARMIS data remains a reliable indicator that BOC special access prices are unreasonable and reflect the lack of competitive alternatives to the BOCs' special access services.

C. Price Cap Rates Far Exceed Forward-Looking, Cost-Based UNE Rates, Rates Offered by Competitors, and Rate-of-Return NECA rates

In their Initial Comments,[216] Commenters demonstrated that the BOCs' price cap rates are unreasonable when compared with any appropriate benchmark.[217] Specifically, the BOCs' rates are significantly higher than cost-based UNE rates, similar offerings by competitors (where competitive facilities exist) and even exceed rate-of-return NECA rates. Moreover, the additional benchmarks that Sprint proposes, which includes rates charged for similar high-bandwidth services that are subject to competition and prices charged in other countries,[218] also confirm that the BOCs' rates far exceed any zone of reasonableness.[219]

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[216] PAETEC *et al.* 1/19/10 Comments, at 67-72.

[217] These benchmarks are the "additional regulatory tools by which to assess the reasonableness of access charges." *Access Charge Reform Order*, ¶ 268. For instance, the Commission stressed that it may "*establish benchmarks based on prices for the interstate access services for which competition has emerged, and use prices actually charged in competitive markets to set rates for non-competitive services or markets*" *Id.* ¶ 268 (emphasis added). The Commission explained that "[c]arriers could be required either to set their rates in accordance with benchmarks or to justify their rates using their cost studies." *Id*.

[218] Sprint 1/19/10 Comments, at 26-30.

[219] *See, e.g., Nader v. FCC*, 520 F.2d 182, 193 (D.C. Cir. 1975) ("In terms of ratemaking, the agency's expertise allows us to accept its judgment after it defines the zone of reasonableness."); *AT&T v. Business Telecom, Inc*., Memorandum Opinion and Order, 16 FCC Rcd 12312, ¶ 29 (2001) (subsequent history omitted) (interpreting *Beehive Telephone Company, Inc.*, Memorandum Opinion and Order, 13 FCC Rcd 12275, ¶ 29 (1998) (*Beehive Telephone)* and explaining that Beehive rests on "the broad discretion that courts have afforded the Commission in 'selecting methods ... to make and oversee rates.' Thus, *Beehive Telephone* reflects the

Qwest acknowledges the need to have appropriate pricing benchmarks and concedes that "the single most widely accepted rule for the governance of the regulated industries is to regulate them in such a way as to produce the same results as would be produced by effective competition, if it were feasible."[220] A comparison of rates offered by competitors (where competitive facilities exist) further demonstrates that price cap rates are excessive and need to be reduced. As noted, the UNE and NECA benchmarks along with the additional benchmarks that Sprint proposes confirm the price cap rates are unreasonable.

While agreeing that regulation should be designed such that it produces the same results as would be produced by effective competition, Qwest ironically contends that the "rates for other providers' services are irrelevant,"[221] and that it would be "irrational to conclude that ILEC rates are 'supracompetitive' simply because they are sometimes higher than some competitors' rates for superficially similar services."[222] Qwest submits that the Commission should take a very selective look at rates by looking only at the ILEC rates in Phase II pricing areas that the Commission determines are competitive.

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understanding that federal agencies with ratemaking authority similar to the Commission's may establish a regulatory scheme that produces a 'zone of reasonableness' for rates, rather than insisting upon a single method of determining whether rates are just and reasonable.") (citations and footnotes omitted).

[220] Qwest 1/19/10 Comments, at 21 (quoting 1 Alfred Kahn, *The Economics of Regulation* 17 (1970); *accord* James C. Bonbright, *Principles of Public Utility Rates* 107 (Columbia Univ. Press 1961) ("Regulation ... is indeed a substitute for competition; and it is even a partly imitative substitute."); *Aeronautical Radio, Inc.* v. *FCC,* 642 F.2d 1221, 1236 (D.C. Cir. 1980) (Wilkey, J., dissenting) (regulation "is essentially a replacement or surrogate for the effects of free competition")).

[221] Qwest 1/19/10 Comments, at 42.

[222] Qwest 1/19/10 Comments, at 24.

Qwest's proposed approach is myopic and unsound. The Commission needs to look at specific buildings and transport routes where competition exists and the standard rates for services offered by the ILECs and competitors in those buildings or on competitive transport routes. The record contains such analysis and demonstrates that the BOCs' rates are not competitive forward-looking levels because they retain market power as they are able to serve many more locations and transport routes than the competitors.

In support of its proposal, Qwest maintains there "is no meaningful way to compare ILEC and CLEC rates without adjusting for a variety of significant *cost differences*," asserting that CLECs "enjoy scale economies" far more than ILECs.[223] Contrary to Qwest's arguments, where competitive facilities exist, both the ILECs and competitive providers should enjoy similar scale economies in their provision of services to those specific locations, and their pricing should reflect that fact. But Qwest's suggestion that a CLEC has more economies of scale compared to a BOC is without any basis in fact. In fact, actual cost studies conducted by some CLECs, including PAETEC, have demonstrated just the opposite with respect to other components of the network because BOCs have significantly greater purchasing power than CLECs.[224] Qwest's claim is contrary to real world facts. Qwest also asserts that "ILEC pricing for the same services may be higher on average because, unlike CLECs, ILECs must maintain ubiquitous networks and provide stand-alone DSn-leve1 pipes to a variety of higher-cost customers that CLECs do not wish to serve, including those in less densely populated locations where scale economies are

[223] Qwest 1/19/10 Comments, at 24 (emphasis in original); *see also id.* at 42.

[224] *See* Letter from Tamar E. Finn, Bingham McCutchen LLP, Counsel for PAETEC, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 01-92, Declaration of Michael Starkey at 3 & Exhibit 2: EXCHANGE ACCESS RATES FOR COMPETITIVE LOCAL EXCHANGE CARRIERS - A Basis for Economically Rational Pricing Policies at 39-40 (filed Oct. 17, 2008).

low or nonexistent."[225] Qwest's argument is nonsensical because an ILEC price cap rates should be set at forward-looking rate levels that assume a competitive marketplace throughout the ILEC's serving area.[226] Moreover, rates could be set at the competitive levels and to the extent a ILEC believes it is under-earning, the ILEC is free to file cost studies to justify a rate increase.

Qwest also contends that "price differences may also reflect *differences in service quality*, including differences in the type of performance guarantees or customer support the ILEC offers that its competitors do not."[227] In a robustly competitive marketplace, competing entities would be expected to offer similar performance guarantees. In fact, competitors of the ILECs will likely offer better performance guarantees and customer support in order to win customers from and be more competitive than the incumbent.

Moreover, as a matter of basic economics, in a competitive marketplace, competing prices for similar services offered by the various providers will be similar regardless of their cost differences. In a truly competitive market, a higher cost producer cannot charge more than competitive prices even though its costs are higher because if it charged more, the higher cost producer would no longer be competitive.

Qwest further asserts that "[a]n apples-to-apples comparison of ILEC rates is also far preferable… from an administrability perspective, because it would avoid intractable disputes about whether a given CLEC service in the sampled market is the 'same' service as the ILEC

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[225] Qwest 1/19/10 Comments, at 24.

[226] Of course, if the ILEC is relieved from rate regulation in certain geographic markets that are found to be competitive as proposed herein, the ILEC would not be required to set special access rates at price cap levels.

[227] Qwest 1/19/10 Comments, at 24 (emphasis in original); *see also id*. at 42.

service in the target market."[228] Contrary to Qwest's claims, determining basic apples-to-apples criteria would not involve intractable disputes because standard rates for basic DS1 and DS3 services could be used for comparison purposes. The Commission need not, however, spend additional time developing this data because it is already in the record and demonstrates that price cap rates are unreasonable. It is apparent that Qwest proposes that the Commission seek more data on this point so that it has more time to assess its exploitive special access rates for a few more years. As ETI explained, for every year that passes without price cap reform, price caps ILECs are able to assess $5 billion in excessive special access charges.[229] Moreover, Qwest's approach to look at ILECs only would fail to accomplish the Commission's goal of setting special access rates at forward-looking levels that are reflective of a truly competitive marketplace. Rather, the rates would be based on ILEC monopolistic rate levels and would permit ILECs to continue to assess excessive rates for special access services. At bottom, the Commission should quickly reject Qwest's self-serving approach[230] to set rates at levels that are not reflective of what would be charged in a competitive market but rather reflect what ILECs wish to charge and can squeeze out of their ratepayers because they are monopolists.

Verizon proposes a different benchmark, suggesting that the Commission consider the AUS Telephone Plant Index ("TPI") as a benchmark to determine that changes in special access costs are not dramatically out of line with changes in special access prices.[231] The Commission

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[228] *Id*. at 42.

[229] Ad Hoc 1/19/10 Comments, Attachment B - LONGSTANDING REGULATORY RULES CONFIRM BOC MARKET POWER: A defense of ARMIS, at A-1.

[230] *See* Qwest 1/19/10 Comments, at 42.

[231] Verizon 1/19/10 Comments, at 44, 49-50 & Attachment B: Declaration of Harold E. West, ¶ 12; *see also* AT&T 1/19/10 Comments, at 56 (citing Hilyer-Makarewicz Decl., ¶ 19).

should quickly reject this proposal, as well. Contrary to Verizon's arguments, the Commission should look at *both costs and revenues* to determine if the BOCs are over earning - not just costs alone. Moreover, the use of the TPI is unhelpful because it does not reflect that TDM technology has likely been fully depreciated and therefore, the cost index is overstated and likely includes costs associated with non-TDM technology and services (i.e. packet-based technology and services) that the BOCs and certain ILECs are not required to offer pursuant to the price cap rules. Moreover, the analysis presented by Verizon is flawed because it increases the costs to account for inflation; however, the record fully demonstrates (as the Commission has previously found), the BOCs' costs are declining because they are more productive than industry as a whole year-over-year.[232]

D. Commenters' requested reforms should be implemented promptly

1. Reinitialization is Critically Necessary Because Forward-Looking Benchmarks Demonstrate that the BOCs' Special Access Rates are Well Above Any Zone of Reasonableness

As Commenters have shown, the Commission's predictive judgment that competition would by now have forced special access prices closer to the Commission's goal of forward-looking economic costs was erroneous.[233] AT&T argues that insufficient evidence exists to show that special access rates are outside a zone of reasonableness.[234]

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[232] PAETEC *et al.* 1/19/10 Comments at 62; Special Access NPRM, ¶ 11 (explaining that "[t]he price cap formula traditionally included a productivity factor (the "X-factor") that represented the extent to which the overall LEC productivity growth rate could be expected to exceed the productivity growth rate of the economy as a whole."); *LEC Price Cap Order*, ¶ 75.

[233] PAETEC *et al.* 1/19/10 Comments at 67; ATX *et al.* 6/13/05 Comments, at 5; *see also* ATX *et al.* 8/8/07 Comments at 39.

[234] AT&T 1/19/10 Comments, at 49. AT&T asserts that the Commission can only "adjust the caps based on returns only where it can be shown that the caps have strayed so far outside the zone of reasonableness as to be beyond any reasonable dispute…." *Id*. Despite the fact there is no such rule that limits how the Commission interprets the Section 201(b) just and reasonable

Contrary to AT&T's assertions, the BOCs' special access rates far exceed the statutory zone of reasonableness. AT&T's arguments ignore the fact that special access rates should fall within a zone that reflects the forward-looking costs of providing services in a competitive marketplace and not within a zone that reflects confiscatory levels a monopolist can extract from its captive customers. The record fully shows that the BOCs' special access rates far exceed a benchmark comparison of forward-looking TELRIC-based rates for functionally equivalent DS1 and DS3 services that would exist if the marketplace were truly competitive.[235] The BOCs' rates also significantly exceed the rates Competitive Access Providers (CAPs) offer for similar services.[236] In fact, "price cap and pricing flexibility rates are typically two to three times higher" than what competitive carriers offer for an equivalent service.[237] Moreover, the rates exceed rate-of-return special access rates of NECA member companies that do not enjoy the BOCs' economies of scale.[238]

If anything, these forward-looking rates are on the high end of any zone of reasonable rates for DS1 or 1.544 Mbps services that Section 201 would allow. Record evidence shows that

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standard and regulates rates, AT&T fails to acknowledge that what is reasonable in the Commission's view is a forward-looking rate and the BOCs' rates are by no means even close to the forward-looking looking rates that would exist if the market were competitive.

[235] *See* ATX *et al.* 8/8/07 Comments, Attachment 4; Sprint 8/8/07 Comments, Declaration of Bridger M. Mitchell, ¶ 57, Exhibit 3; XO *et al.* 8/8/07 Comments, at 17-20 & Attachment 2; *see* Letter from Brett Heather Freedson, Kelly Drye & Warren, LLP, to Marlene Dortch, Secretary, FCC, WC. Docket No. 05-25, RM-10593 (filed Aug. 10, 2007) (attaching an errata); Letter from David Lawson, Sidley Austin Brown & Wood LLP, to Marlene H. Dortch, Secretary, FCC RM-10593, at Declaration of M. Joseph Stith (dated Oct. 4, 2004) (filed in RM-10593 Dec. 7, 2004).

[236] *See, e.g.*, PAETEC et al. 1/19/10 Comments at 70-71; TWTC 7/9/09 *Ex Parte*, at 2, 4, 9, & 21; Global Crossing 8/8/07 Comments, Declaration of Janet S. Fischer, ¶ 6, Tables 5-6; WILTEL 7/29/05 Comments at 5, 17-20 and Exhibit 1.

[237] Global Crossing 8/8/07 Comments, Declaration of Janet S. Fischer, ¶ 6.

[238] PAETEC *et al.* 1/19/10 Comments, at 71.

Verizon and AT&T are charging their *retail customers* between $54.99 and $35.00 per month for services reaching much higher speeds of 15 Mbps and 6 Mbps, respectively.[239] A forward-looking cost structure that applies to the BOCs' DS1 special access services should result in wholesale rates that are *lower, not higher* than what the BOCs currently charge their retail customers for comparable services. For these reasons, reinitializing special access rates is imperative.

2. Reinitializing Special Access Rates at Cost-Based, Forward-Looking Levels is Appropriate

Since the Commission has already concluded that "access charges should ultimately reflect [forward-looking] rates that would exist in a competitive market,"[240] as proposed in earlier comments, special access rates should be reinitialized and set at these levels.[241] The BOCs offer several arguments against reinitialization, none of which are availing. AT&T argues that such a rate investigation would trigger complex proceedings.[242] It contends, among other things, the Commission would have to establish joint and common cost allocations along with a new rate-of-return, which would be difficult if not impossible to defend.[243] In making these

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[239] Sprint 1/19/10 Comments, at 28 n.91, Declaration of Bridger M. Mitchell, ¶ 112; *see also* Sprint 8/8/07 Comments, at 23-24.

[240] *See Access Charge Reform Order*, ¶ 42.

[241] PAETEC *et al.* at 75; ATX *et al.* 6/13/05 Comments at 18; ATX *et al.* 8/8/07 Comments at 39.

[242] AT&T 1/19/10 Comments, at 72.

[243] AT&T 1/19/10 Comments, at 62 and 67. AT&T asserts that trying to "establish and justify a 'reasonable' rate of return for special access services as of 2010 would be an intractable and hopelessly arbitrary exercise." AT&T 1/19/10 Comments, at 64. The Commission has, however, established a rate-of-return in the past and can so again. *See, e.g., Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers,* CC Docket No. 89-624, Order, 5 FCC Rcd 7507, ¶ 1 (1990) (subsequent history omitted); *see also Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the*

arguments,[244] AT&T implicitly acknowledges that commissions in virtually every state, including the Wireline Competition Bureau with respect to the Virginia arbitration, previously faced and were able to handle the complexities associated with establishing forward-looking TELRIC rates.[245] Hence, the issues are far from insurmountable and problematic.[246] Indeed, since the Commission was established, rate regulation of interstate communications (including interstate special access services) has been one of its basic responsibilities.[247]

Furthermore, even though a full and thorough Commission investigation of the BOCs' special access rates would entail certain costs and burdens, there is no question they would be justified, especially since the record shows the BOCs' overcharges yielded $8.31 billion in excessive special access revenues or $22.77 million in overcharges per day in 2006 and that their excessive special access rates were estimated between 2007 and 2009 to deprive the US

Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc., and for Expedited Arbitration, CC Docket Nos. 00-218, 00-251, Memorandum Opinion and Order, 18 FCC Rcd 17722, ¶¶ 58-104 (WCB 2003) (establishing cost of capital to be used in determining UNE rates).

[244] AT&T argues that the protracted TELRIC proceedings demonstrate how difficult and contentious any attempt to determine forward-looking costs would be. AT&T 1/19/10 Comments, at 72-73. For this reason, as discussed below, the Commission could utilize UNE rates to establish reasonable rates for special access services.

[245] AT&T 1/19/10 Comments, at 72-73.

[246] Moreover, if AT&T, Verizon, and Qwest were to file cost studies with the Commission, this approach would be much less administratively burdensome than the state TELRIC proceedings. There would only be three proceedings, rather than the fifty or more proceedings before state commissions that took place when UNE rates were first established.

[247] Should the Commission conclude that the burden of establishing rates based on forward-looking costs was undue, it could establish special access prices at state-approved TELRIC rates for comparable UNEs, or at such rates plus a factor. Such an approach would take advantage of the effort that has already been undertaken in TELRIC UNE cost proceedings throughout the nation. Moreover, the Commission has reviewed the rates in the context of 271 proceedings and found that they were within a forward-looking zone of reasonableness.

economy of some 234,000 new jobs and GDP growth in the range of $66 billion.[248] The more time that passes, the more these frightening numbers increase.

AT&T also asserts that any re-initialization would be arbitrary.[249] This assertion flies in the face of the careful and studied manner in which the Commission has addressed special access rate regulation in the last fifteen to twenty years. As early as 2002, when the Commission opened RM-10593, it became apparent that the Commission's special access pricing rules were not having the intended effect and evidence submitted since then further demonstrates the Commission's predictive judgment failed miserably. A course-correction required by the wide divergence between expectations and results is by no means "arbitrary," and is in fact the Commission's duty.[250] Moreover, there are significant economic benefits in doing so.[251] Any

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[248] Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at i; ETI 2/11/10 Report, at 33-34.

[249] AT&T 1/19/10 Comments, at 50.

[250] *See Bechtel v. FCC*, 957 F.2d 873, 881 (D.C. Cir. 1992) ("The Commission's necessarily wide latitude to make policy based upon predictive judgments deriving its general expertise implies a correlative duty to evaluate its policies over time to ascertain whether they work – that is, whether they actually produce the benefits the Commission originally predicted they would.") (citations omitted); *ACLU v. FCC*, 823 F.2d 1554, 1565 (D.C. Cir. 1987) (the D.C. Circuit has specifically "emphasize[d] the need for the Commission to vigilantly monitor the consequences of its rate regulation rules" where, as here, "the Commission itself has recognized the tentative nature of its predictive judgments."); *see also BellSouth v. FCC*, 469 F.3d 1052, 1060 (D.C. Cir. 2006) (finding that "the deference owed agencies' predictive judgments gives them no license to ignore the past when the past relates directly to the question at issue.").

[251] *See* ETI 2/11/10 Report, at 33-34; Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness, at i; *see also* Letter from Brian R. Moir, Partner, Moir & Hardman, to Marlene H. Dortch, Secretary, FCC, RM-10593 (filed June 12, 2003) (attaching macroeconomic analysis of the impact on the U.S. economy if excessive special access prices were lowered to reasonable levels. This study demonstrated that by reducing special access rates to levels that would produce an 11.25% return would result in immediate positive benefits by adding $14.5 billion to the U.S. economic output (Gross Domestic Product) and by creating 132,000 new jobs in the first two years.).

reasonable regulated business should realize that, far from being arbitrary, such an action is inevitable.[252]

The BOCs also argue that any re-initialization and re-regulation would be inconsistent with the core premises of price cap regulation and will undermine the credibility of the incentive-based system.[253] This claim is ironic because, as discussed initially, the credibility and effectiveness of an incentive-based system has been destroyed by the BOCs themselves. While price cap regulation was designed to "replicate[] efficiency incentives of a competitive market",[254] this goal has unfortunately not been realized. Instead, price cap regulation, combined with pricing flexibility, has rewarded monopolistic behavior and punished consumers with unreasonable special access rates, adversely affecting the entire economy.[255]

Finally, in arguing that re-initialization and re-regulation would be inconsistent with the core premises of price cap regulation, the BOCs imply that re-initializing prices will not inspire them to operate more efficiently.[256] This implicit claim is also unavailing. Re-setting rates after

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[252] AT&T also implicitly argues the Commission cannot reinitialize special access rates in isolation and would have to concurrently take a fresh look at switched access rates, where ARMIS returns are very low. AT&T 1/19/10 Comments at 67. Contrary to this implicit claim, the Commission can establish switched access and special access rates independent from each other. Just as AT&T filed the Petition for Rulemaking back in 2002 that initiated this proceeding, AT&T can likewise file another one requesting the commencement of a rulemaking proceeding for switched access rates.

[253] *See, e.g.*, AT&T 1/19/10 Comments, at 5, 10-11, 50-51; Verizon 1/19/10 Comments, at 43-44; Qwest 1/19/10 Comments, at 2, 4, 48.

[254] *See, e.g.*, AT&T 1/19/10 Comments, at 51.

[255] *See* Ad Hoc 8/8/07 Comments, Appendix 1: SPECIAL ACCESS OVERPRICING AND THE US ECONOMY - How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness.

[256] *See, e.g.*, AT&T 1/19/10 Comments, at 52 (asserting that "[t]hese incentives for increased efficiency, investment, and innovation would not exist, however, unless the ILECs could keep

19 years, based on current forward-looking costs (rather than the BOCs' actual costs) preserves the BOCs' incentive to reduce their costs below the re-initialized rates and hence increase their margins consistent with the incentives contemplated when the price cap formulation was adopted in 1991.[257] Moreover, in economic terms, it should be incentive enough for any business to achieve rates-of-return that are realistically obtainable in a competitive marketplace. Only a monopolist can expect more. Indeed, the fact BOCs have such expectations is further evidence that they face little or no competition in the special access market.

3. The Record Supports Modifying the X-Factor

Once special access rates are reinitialized, as proposed in earlier comments, the Commission should include all special access rates under a modified price cap regulatory framework[258] and make a productivity-based X-factor a key feature of such new rules. Because the BOCs threaten to reduce their investment in network efficiencies in the face of new price caps, it is even more important that the Commission reinstitute an X-factor to ensure that BOCs capitalize on the technological advancements of their suppliers so that their special access productivity improves.[259]

AT&T contends any attempt to determine a new X-factor or use productivity studies to reinitialize the price caps is unnecessary and would produce an arbitrary result.[260] Contrary to AT&T's claims, the record fully supports modifying the X-factor because, as discussed

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the increased profits that these improvements in efficiency make possible.") at 50 & 63; Verizon 1/19/10 Comments at 43-44; Qwest 1/19/10 Comments at 48.

[257] *See, e.g., Special Access NPRM*, ¶ 11.

[258] ATX *et al.* 6/13/05 Comments, at 24-32; ATX *et al. 8/8/07* Comments, at 43-48; PAETEC *et al.* 1/19/10 Comments, at 76-80.

[259] *See also* ATX *et al.* 7/29/05 Comments, at 43-44.

[260] AT&T 1/19/10 Comments, at 74.

previously, BOCs enjoy productivity levels significantly greater than the economy as a whole. As shown previously, it would be inappropriate to set the X-factor at the inflation rate because BOC customers would not benefit from the reduced costs associated with above-average productivity gains.[261]

The ETI study presented in 2005 demonstrated that an X-factor of approximately 11 percent would be appropriate.[262] Moreover, the 2007 study that Sprint submitted, updating the 2005 ETI study, shows that the BOCs' interstate special access productivity continues to outstrip productivity gains in the economy as a whole and supports an X-factor of 16.95 percent.[263] Contrary to AT&T's claims, these proposed X-factors are fully supported and are by no means arbitrary. While AT&T in the past has argued the ETI study is unsound because it relies on historical ARMIS data and assumes an 11.25 percent rate-of-return, its criticisms of ARMIS data are unavailing as shown elsewhere herein and the 11.25 percent rate-of-return should (if anything) be reduced, which in turn would produce an even higher X-factor. The productivity gains associated with the BOC mergers, which have yet to be taken fully into account, would as well.[264]

AT&T further claims that if the Commission attempted to design an X-factor, it would face "endless proceedings and litigation."[265] AT&T conveniently ignores the fact that an X-factor had been in effect for seven years prior to *United States Telecom Ass'n v. FCC*, 188 F.3d

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[261] PAETEC *et al.* 1/19/10 Comments at 62-63; ATX *et al.* 8/8/07 Comments, at 43-44; ATX *et al.* 7/29/05 Comments, at 45-46.

[262] Ad Hoc 7/29/05 Reply Comments, Reply Declaration of Susan M. Gately, ¶ 8 & ¶ 10.

[263] Sprint 8/8/07 Comments, Exhibit 2, at 1.

[264] ATX *et al.* 8/8/07 Comments, at 19-21.

[265] AT&T 1/19/10 Comments, at 73-74.

521 (D.C. Cir. 1999)) apparently without crippling the industry. Moreover, the D.C. Circuit did not condemn the concept of an X-factor, nor the formula by which it was calculated. Rather, it criticized the Commission's lack of explanation for the process by which it selected the data to enter into the formula.[266] This by no means amounts to repudiation of the X-factor concept, nor do any of these criticisms portray a fatal problem. The Commission established legally sustainable X-factors in the past and can do so again.

Moreover, contrary to AT&T's contention, rules governing any interim prices need not include a definitive analysis of LEC productivity if an interim approach incorporated an X-Factor. The *CALLS Order* incorporated an X-Factor for interstate special access even though it had nothing to do with productivity. The Commission stated:

> By adopting the reasonable approach set forth in the CALLS Proposal, which treats the X-Factor not as a productivity estimate but as a method to reduce rates to certain levels, we expect to end the debate over the appropriate size of the X-Factor now and for the next five years for participating price cap LECs.[267]

Again, the Commission may take the same approach here. If a price cap LEC does not want to adjust prices according to an X-Factor, it may establish just and reasonable prices based on forward-looking cost.

Consistent with the Commission's justification of the X-factor in the *LEC Price Cap Order*, the Commission should re-impose a productivity X-factor offset in the price cap formula

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[266] Specifically, the court determined that the Commission should have explained (1) why outlying historical productivity data was unreliable or its use inappropriate, (2) how it determined that there was an upward trend in the historical data, and (3) why it accepted estimates of the range of reasonableness based on methodologies that it had previously discredited. *United States Telecom Ass'n v. FCC*, 188 F.3d 521, 525-526 (D.C. Cir. 1999).

[267] *Calls Order*, ¶ 40.

to ensure that rates continue to decline relative to the measure of inflation, GNP-PI.[268] As proposed, the Commission should, at a minimum, apply the X-factor prospectively.[269]

(3) Do the Commission's Price Cap and Pricing Flexibility Rules Ensure that the Terms and Conditions in Special Access Tariffs and Contracts are Just and Reasonable?

As discussed in the Commenters' Initial Comments, the record in this proceeding establishes that the Commission's price cap and pricing flexibility rules have not prevented the BOCs from imposing onerous and unreasonable terms and conditions on the purchase of special access services.[270] To be clear, not every volume and term commitment is unjust or unreasonable in the abstract -- on the contrary, such arrangements are commonly used in many industries,[271] and they can play a valuable role in the telecommunications industry as well. But the touchstone must be whether such terms and conditions reflect the voluntary, mutually beneficial agreement of a carrier and a customer, rather than being the product of a market in which customers are compelled to accept such terms and conditions in the absence of meaningful competitive alternatives.

AT&T and Verizon claim that the terms and conditions in their special access contracts and tariffs cannot be unjust and unreasonable because the markets in which they arose are competitive. AT&T asserts, for example, that the terms and conditions reflect those commitments that a customer "voluntarily *chose*," that these "choices" were made "in a

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[268] *LEC Price Cap Order*, ¶ 75.

[269] *See* PAETEC *et al.* 1/19/10 Comments, at 76.

[270] PAETEC *et al.* 1/19/10 Comments, at 80-84 (citations omitted).

[271] *See* TWTC 7/9/09 *Ex Parte*, at 22 (citing Decl. of Michael D. Pelcovitz, at 7, attached to Reply Comments of WorldCom, RM-10593 (filed Jan. 23, 2003) (stating that volume and term commitments "do not have exclusionary effects in a competitive environment, because each seller is able to supply a customer's entire needs. Exclusionary or anticompetitive possibilities only arise when one firm, the incumbent monopolist, can supply each customer's entire demand.")).

competitive context," and that the customer's decision "represented a judgment that the ILEC's competitors' prices were not sufficiently attractive to warrant acceptance of that offer."[272] Verizon likewise contends that discount plans of the kind offered by the BOCs "are a common practice in a number of industries that display vigorous competition, which suggests that such agreements are not generally harmful."[273]

These arguments fail because they are circular in nature, contending that terms and conditions cannot be anticompetitive because they assertedly arose in competitive markets. Whether the markets for special access services are competitive is, however, one of the key disputed issues in this proceeding, one on which Commenters and many others have voiced substantial disagreement with AT&T and Verizon. As described at length above and in Commenters' Initial Comments, the record in this proceeding is replete with evidence showing that the relevant special access markets can hardly be considered subject to the kind of "vigorous competition" cited by Verizon in its defense of these terms and conditions, nor does the evidence support AT&T's claim that customers "freely agreed to them in a market in which they had choices."[274] Indeed, with their ubiquitous reach, monopoly status on many routes, and ability to

[272] AT&T 1/19/10 Comments, at 77 (emphasis in original).

[273] Verizon 1/19/10 Comments, at Attachment A: Declaration of Michael D. Topper, ¶ 66.

[274] AT&T 1/19/10 Comments, at 81. AT&T further argues that the Commission "expressly rejected" a "lock-in" theory in first establishing pricing flexibility. *Id*. (citing Fifth Report and Order and Notice of Proposed Rulemaking, *Access Charge Reform*, 14 FCC Rcd 14221, ¶ 125 (1999)). But the Commission's finding that risks with "lock-ins" were "less likely" to arise was premised upon the collocation-based, MSA-wide indicators of competition that few, if any, bother to defend any longer. With it now being clear that these triggers failed to provide an accurate snapshot of competition, this is all the more reason to take a closer look at whether an absence of real competition has permitted the BOCs to abuse their market power in areas that the existing regime has deemed competitive.

leverage market power with customers and even building owners,[275] the BOCs occupy a position of substantial strength and are able to impose nearly any demand that they want in connection with volume and term commitments. Numerous examples of such terms and conditions were cited in or provided with the Commenters' Initial Comments, ranging from required conversion of UNEs and prohibitions on commingling to demands that a certain volume of circuits be migrated from another carrier to the BOC or tying of interoffice transport and channel terminations.[276] In addition, even if the relevant markets were truly competitive, the Commission cannot take it on faith that terms and conditions arising with those markets are necessarily just and reasonable.

Thus, rather than accepting at face value the BOCs' claims that these markets are competitive and that thus "there is nothing to see here," the Commission should adopt two sets of rules that will ensure that all terms and conditions are just and reasonable. First, the Commission should implement a series of specific prohibitions on terms and conditions that: (1) require the

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[275] *See* Level 3 1/19/10 Comments, at 16-18 (discussing the various complications in deployment of lateral facilities); TWTC 7/9/09 *Ex Parte*, at 20 (discussing the incentives of a monopoly provider with respect to offering proportional or relative discounts "in order to induce customers to agree to exclusionary provisions"); Letter from Tamar Finn, Counsel for PAETEC Communications, Inc., to Marlene Dortch, Secretary, FCC WC Dockets Nos. 07-135 and 05-25, at 2 (filed May 29. 2009) (discussing the incumbent's ability to secure exclusive contracts with building owners).

[276] *See* Comments of TDS Metrocom, *et al*., WC Docket No. 05-25, GN Dockets Nos. 09-47, 09-51, 09-137, RM-10593, RM-11358, at Attachment A (filed Nov. 4, 2009); PAETEC *et al.* 1/19/10 Comments, at Exhibit 2. On page 82 of the PAETEC *et al.* 1/19/10 Comments, a chart categorizing various AT&T's anticompetitive terms and conditions appearing in one of AT&T's tariffs was referenced as being attached to the comments as Exhibit 2. The AT&T chart was not provided in Exhibit 2 to the PAETEC *et al.* 1/19/10 Comments (as Exhibit 2 only contained a chart depicting sample Verizon tariff terms and conditions), but rather was submitted earlier in this proceeding as noted correctly in footnote 278 of the PAETEC *et al.* 1/19/10 Comments. *See* Comments of TDS Metrocom, *et al.*, WC Docket No. 05-25, GN Docket Nos. 09-47, 09-51, 09-137, RM-10593, RM-11358, at Attachment A (filed Nov. 4, 2009).

purchase of a specified quantity of other services to obtain discounts or credits on channel terminations; (2) mandate that channel terminations represent only a limited percentage of the customer's total spend with the BOC; (3) apply ratios limiting the amount of non-special access services a customer can purchase to receive discounts or credits; (4) require the purchase of products in multiple geographic markets to obtain discounts or credits; (5) compel the customer to refrain from any purchases of UNEs or other specified services (or the commingling of such services with special access services); and (6) mandate the migration of a certain percentage of total spend or quantity of circuits from a BOC's competitor as a condition to obtaining discounts or credits. Second, the Commission should adopt more general and overarching rules that will minimize the opportunity for BOCs to implement new and creative ways of evading the intent of specific prohibitions such as those above; specifically, the Commission should prohibit any arrangements that: (a) tie a BOC's monopoly and competitive services; and/or (b) result in any cross-subsidization through use of higher rates on services that are not subject to competition to "fund" discounts or credits applicable to competitive services. To the BOCs' point that volume and term commitments can play a mutually beneficial role for customers and suppliers, rules such as those described above would not preclude the use of volume and term commitments or other creative purchase plans in competitive markets -- but they would ensure that a BOC cannot use market power to "lock up" specific routes prior to competitive entry and/or use tying arrangements to deter customers from purchasing competitive services (where available).

III. CONCLUSION

The Commission should promptly grant the Commenters' requested relief.

Respectfully submitted,

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Dated: February 24, 2010